

COUNCIL OF
FINANCIAL
REGULATORS

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1. COUNCIL OF FINANCIAL REGULATORS

The Council of Financial Regulators is the co-ordinating body for Australia's main financial regulatory agencies: the Reserve Bank of Australia (RBA), which chairs the Council; the Australian Prudential Regulation Authority (APRA); and the Australian Securities and Investments Commission (ASIC).

The Council's role is to contribute to the efficiency and effectiveness of financial regulation by providing a high-level forum for co-operation and collaboration among its members. It operates as an informal body in which members are able to share information and views, discuss regulatory reforms or issues where responsibilities overlap and, if the need arises, co-ordinate responses to potential threats to financial stability. These arrangements provide a flexible, low-cost approach to co-ordination among the main financial regulatory agencies. The Council is non-statutory and has no regulatory functions separate from those of its members.

Membership of the Council comprises two representatives – the chief executive and a senior representative – from each of the three regulatory agencies. The Chairman is the Governor of the RBA, and the RBA provides the Council Secretariat. The Council met for the first time in May 1998 and currently meets about once every quarter.¹ The Council's charter and administrative arrangements are shown in the box below and in Appendix A.

Council Activities in 2001

The year 2001 was one of considerable turmoil in the global economy. International economic conditions were at their weakest for a decade and equity markets underwent substantial corrections. A succession of severe shocks in the latter part of the year – the terrorist attacks of September 11, the collapse of Enron and the largest sovereign debt default in the case of Argentina – further tested the resilience of the global financial system. Despite the external pressures, the Australian financial system continued to perform strongly. These various developments provided the backdrop to the Council's activities in 2001.

On the domestic front, the remaining plank of regulatory reform recommended by the Financial System Inquiry (the Wallis Committee) fell into place when the *Financial Services Reform Act 2001*, which deals with the regulation of financial markets, was passed into law. The reform agenda, however, is by no means complete: strengthening

¹ The Council is the successor to an earlier co-ordinating body, the Council of Financial Supervisors, which met between 1992 and 1998.

the prudential framework for general insurance and superannuation remain important priorities. Other important priorities include improving disclosure and quality of financial services to investors and consumers and improving corporate conduct and continuous disclosure to the markets. The involvement of Council members in financial sector reform is outlined in Chapter 2.

On the external front, the global financial system was able to weather the severe shocks of 2001 but its capacity to absorb any additional strains remains a key issue for policy makers. The task of strengthening this system, which has been underway since the Asian crisis a few years earlier, has therefore gained greater impetus. The response of Council members to the financial shocks and their participation in global reform efforts, which the Council itself helps to co-ordinate, is covered in Chapter 3.

Council Charter

The Council of Financial Regulators aims to facilitate co-operation and collaboration among its members, the main regulators of the Australian financial system – the Reserve Bank of Australia, the Australian Prudential Regulation Authority and the Australian Securities and Investments Commission. Its ultimate objective is to contribute to the efficiency and effectiveness of regulation.

The Council provides a forum for:

- sharing information and views among its members, and liaison with other regulators and agencies;
- harmonising regulatory and reporting requirements, paying close attention to the need to keep regulatory costs to a minimum;
- identifying important issues and trends in the financial system, including the impact of technological developments; and
- co-ordinating regulatory responses to actual or potential instances of financial instability, and helping to resolve any issues where members' responsibilities overlap.

2. AUSTRALIA'S FINANCIAL REGULATORY FRAMEWORK

Summary of Framework

Australia's current financial regulatory framework, the main elements of which were introduced on 1 July 1998, arose out of the findings of the Financial System Inquiry (the Wallis Committee). The Inquiry recommended wide-ranging reforms to the structure of financial regulation, designed to achieve a more competitive, efficient and flexible financial system.

The regulatory framework consists of three agencies, each with specific functional responsibilities:

- the Australian Prudential Regulation Authority (APRA), which has responsibility for prudential supervision;
- the Australian Securities and Investments Commission (ASIC), which has responsibility for market integrity and consumer protection across the financial system; and
- the Reserve Bank of Australia (RBA), which has responsibility for monetary policy, overall financial system stability and regulation of the payments system.

The **Australian Prudential Regulation Authority** is an integrated prudential regulator responsible for deposit-taking institutions (banks, building societies and credit unions) as well as friendly societies, life and general insurance and superannuation.² APRA is charged with developing prudential policies that balance financial safety and efficiency, competition, contestability and competitive neutrality.

Deposit-taking institutions are regulated by APRA under a single licensing regime and are covered by the same 'depositor preference' provisions of the *Banking Act 1959*. This legislation gives APRA the power to act decisively in the interests of depositors, including the power to revoke licences, to make prudential standards or issue enforceable directions, to appoint an investigator or statutory manager to an authorised deposit-taking institution (ADI) in difficulty or take control of the institution itself. If the difficulties prove intractable, APRA has the power to wind-up the institution and distribute its assets.

2 APRA regulates the compliance of superannuation funds with the prudential regulation and retirement income provisions of the *Superannuation Industry (Supervision) Act 1993*, while ASIC has responsibility for the other provisions. The Australian Taxation Office has responsibility for the regulation of excluded funds (which have less than five members).

Under the ‘depositor preference’ provisions of the *Banking Act 1959*, depositors have first claim to the assets of an ADI in a wind-up. To support depositors’ interests, all ADIs are required to hold assets in Australia at least equal to their deposit liabilities in Australia. These arrangements, however, do not confer any form of guarantee of depositors’ funds, and depositors have no recourse to APRA or the Government.

As in the case of ADIs, where the financial weakness of a life company, general insurer, friendly society or superannuation fund could have a detrimental effect on the interests of members and policyholders, APRA may intervene in the management of the troubled entity. In the case of superannuation, the Treasurer can compensate members of a fund for losses due to fraudulent conduct or theft if the public interest requires it. The assistance can be funded either from Consolidated Revenue or by levying other funds within the industry. Again, however, members’ and policyholders’ entitlements are not guaranteed by either APRA or the Government.

The **Australian Securities and Investments Commission** administers and enforces a range of legislative provisions relating to financial markets, financial sector intermediaries and financial products, including investments, insurance, superannuation and deposit-taking activities (but not lending). ASIC’s aim is to protect markets and consumers from manipulation, deception and unfair practices and, more generally, to promote confident participation in the financial system by investors and consumers. With this in mind, ASIC also seeks to promote honesty and fairness in company affairs and securities and futures markets through adequate and timely disclosure of market information. ASIC also:

- develops policy and guidance about the laws which it administers;
- licenses and monitors compliance by participants in the financial system; and
- provides comprehensive and accurate information on companies and corporate activity.

As part of its consumer protection role, ASIC also monitors and assesses compliance with the *Code of Banking Practice*, the *Credit Union Code of Practice*, the *Building Society Code of Practice* and the *Electronic Funds Transfer Code of Practice*. ASIC also supervises a number of industry-based alternative dispute resolution schemes.

ASIC will also implement the provisions of the *Financial Services Reform Act 2001* which introduces a new financial services disclosure and licensing regime.

The **Reserve Bank of Australia** has responsibility for monetary policy and for overall financial system stability. The RBA has no obligation to protect the interests of bank depositors; rather, its task is to deal with threats to financial stability which have the potential to spill over to economic activity and consumer and investor confidence. In

the event of such threats, the RBA retains its discretionary role of 'lender of last resort' for emergency liquidity support. If it were to provide such support, the RBA's preference would be to make funds available to the market as a whole through its domestic market operations. In certain circumstances, however, the RBA would be prepared to lend directly to a financial institution facing liquidity difficulties. The institution would have to be one supervised by APRA; would have to be solvent; and the failure to make its payments would have to pose a threat to overall financial system stability. APRA's judgments about the fundamental soundness of a financial institution in distress would be critical to any RBA support.

The RBA, under the auspices of its Payments System Board, also has a mandate to promote the safety and efficiency of the Australian payments system, and has the backing of strong regulatory powers. If the RBA, for example, assesses there is scope to improve access to, or the efficiency or safety of, a particular payment system, it can 'designate' that system as being subject to its regulation. It may then, in the public interest, impose an access regime on that system and/or set standards for efficiency or safety. The Government envisaged that these powers would be exercised within a broad co-regulatory approach, with safeguards for private-sector operators. The RBA also remains responsible for conducting Exchange Settlement Accounts for participants in the payments system and in 1999 it announced new arrangements which liberalised access to these Accounts.

Annual Reports and Internet sites of the individual Council members (see page 22) contain further details about their responsibilities and activities.

Developments in the Regulatory Framework

Since its establishment, APRA has given priority to developing a more integrated and harmonised supervisory framework for ADIs, and a comprehensive framework for the prudential supervision of conglomerate groups that include an ADI. These frameworks are now largely complete.

APRA has also undertaken a significant overhaul of the prudential framework for the **general insurance** industry, which had been little changed since the *Insurance Act 1973* was introduced. The emergence of substantial losses in the industry over recent years reinforced the need for reform and added urgency to the process. Accordingly, APRA developed, published for comment and, following industry consultation, recommended to the Government a comprehensive and modern set of reform proposals for the prudential supervision of general insurance companies. These proposals were approved by the Government in November 2000 and amendments to the *Insurance Act 1973* to give effect to new prudential standards were passed by

Parliament in August 2001. The final new prudential standards were tabled in Parliament in February 2002 and come into force on 1 July 2002. Some key aspects of the new standards follow.

Under the previous regime, general insurers had considerable discretion in how they valued their insurance liabilities. APRA's new *Liability Valuation Standard* seeks to ensure that insurers value their insurance liabilities in a realistic and consistent manner, drawing on written advice from an approved actuary. The Board of Directors of an insurance company will have the power to override the actuary's advice but should disclose this in the company's published annual financial accounts. The standard also requires that insurers include a risk margin to ensure that the value of insurance liabilities is established at a sufficient level.

The *Capital Adequacy Standard* aims to ensure that insurers can meet their insurance obligations under a wide range of circumstances by maintaining at least a minimum amount of capital. The standard defines the minimum capital requirement to be at least \$5 million (up from \$2 million); above \$5 million, regulatory capital requirements are risk-based. Insurers writing long-tail liability business, for example, face greater uncertainty and need more capital than do those writing short-tail property business. The standard will mean an increase in regulatory capital requirements on average, but the industry as a whole already holds a significant buffer of capital over the minimum requirements.

The *Risk Management Standard* aims to ensure that an insurer is well managed, has access to appropriate independent advice and has systems for identifying, managing and monitoring risks. The Board of Directors of an insurer must develop a risk management strategy aimed at mitigating all material financial and operational risks. Each insurer also needs to ensure that persons occupying key positions have the degree of probity and competence commensurate with their responsibilities. The standard sets out various requirements as to the composition of the Board and Audit Committee. In addition, each insurer must provide APRA with an annual Board Declaration certifying that it has complied with all relevant legislative and prudential requirements and addressed all material risks.

Under the *Reinsurance Arrangements Standard*, the Board of Directors of an insurer must develop, implement and maintain a high-level reinsurance management strategy appropriate to the operations of the insurer. The strategy needs to have regard to diversification and the creditworthiness of counterparties and consider the extent and use of financial reinsurance and alternative risk transfer products.

APRA's new liability valuation and capital adequacy standards are aimed at strengthening the ability of general insurers to meet their policyholder obligations, while the new risk management and reinsurance standards are aimed at good governance.

In combination, the new prudential standards should significantly reduce the likelihood of failures in the general insurance industry.

The appropriate regulatory framework for **superannuation** became a major reform issue in 2001. The triggers were financial losses experienced by a small number of superannuation funds and a growing recognition of the need to improve existing legislative and prudential arrangements to deal with weaknesses, in particular, in small and medium-sized funds.

Early in 2001, amendments to the *Superannuation Industry (Supervision) Act 1993* (SIS Act) gave APRA an array of more effective enforcement options. Various “fault liability” offence provisions, where the prosecution needed to prove that an act or omission was reckless or deliberate, were changed to “strict liability”. APRA now has the power to declare persons to be disqualified if they have been associated with breaches of the superannuation legislation of such seriousness or frequency that APRA considers they should be disqualified; persons can also be disqualified if APRA determines that they are otherwise not ‘fit and proper’ to fulfil such roles. APRA also now has the power to accept an enforceable undertaking under the SIS Act. Other amendments improved the capacity of a replacement trustee appointed by APRA to take control of the affairs of a superannuation fund, and make it an offence for persons without the requisite qualifications to claim they are an approved auditor or actuary. APRA has exercised these powers several times and has noted a greater willingness on the part of trustees to address matters of serious concern in a prompt and effective manner.

APRA has contributed significantly to a number of recent reviews and inquiries into the superannuation industry. These include the Productivity Commission’s National Competition Policy review of certain superannuation Acts; various reviews by the Senate Select Committee on Superannuation and Financial Services chaired by Senator Watson; and the Superannuation Working Group established by the Federal Government to conduct public consultation in relation to an Issues Paper on “Options for Improving the Safety of Superannuation”. In its submissions, APRA has highlighted the challenges it faces in supervising superannuation – in particular, the large number of superannuation funds involved and the lack of some key supervisory powers under the current legislation.

APRA supports the introduction of a licensing regime for all APRA-regulated superannuation funds under which APRA would have the power to grant and revoke licenses. APRA has also argued for powers to make prudential standards in superannuation similar to its powers in other regulated sectors. APRA has outlined a number of areas where standards could be appropriate, including superannuation fund investments, risk management, capital adequacy and outsourcing.

The final element of the reform agenda promoted by the Financial System Inquiry – dealing with the regulation of **financial markets** – was bedded down when the *Financial Services Reform Act 2001* (FSR Act) was passed by Parliament in August 2001. The new arrangements came into force on 11 March 2002, with a two-year transition period. ASIC is responsible for implementing the FSR Act. It has dedicated a significant amount of resources to the implementation of the Act in order to enable a smooth and effective transition to the regime, which is essential to the integrity and confidence of markets.

The FSR Act introduces a streamlined regulatory regime for market integrity and consumer protection across the financial services industry. It provides for a harmonised licensing, disclosure and conduct framework for financial service providers, and a single statutory regime for financial product disclosure. At the same time, the framework allows for flexible treatment of different financial products where appropriate (eg basic deposit products will be subject to less intensive regulation than more complex investment products).

The multiple routes to licensing of securities and futures exchanges, and of clearing and settlement systems, have been replaced by a single licensing regime for an Australian financial market and for a clearing and settlement facility. Under the new arrangements, licensees have primary responsibility for the operation of markets and of clearing and settlement facilities; “the responsible Minister” has overall responsibility for licensing such entities. ASIC is empowered to advise the Minister on licensing matters and is also required to undertake assessments of the compliance of market and facility licensees with their legislative obligations, and to take enforcement action where necessary.

Under the new arrangements, the RBA has responsibility for ensuring that clearing and settlement facilities conduct their affairs in a way that is consistent with overall financial system stability. As part of this role, the RBA has the power to set and monitor compliance with financial stability standards for clearing and settlement facilities. ASIC has responsibility for all other matters relating to these facilities, such as those covering corporate governance, market integrity and investor protection, and for enforcing compliance with the RBA’s standards if this becomes necessary. The RBA and ASIC signed a Memorandum of Understanding (MOU) in March 2002 which sets out a framework for co-operation between the two agencies in relation to licensed clearing and settlement facilities. The MOU is intended to promote transparency, help prevent unnecessary duplication of effort and minimise the regulatory burden on facilities; it covers information sharing, notification and other arrangements intended to achieve these aims.

As part of its role in implementing the FSR Act and giving guidance on implementation, ASIC prepared a suite of policies and process guides and a licensing kit. ASIC also

conducted industry consultation visits, ASIC Speaks seminars and provided extensive information on its web site.

A new *Electronic Funds Transfer Code of Conduct* was also launched by ASIC. The Code covers all forms of electronic banking, including telephone and internet banking and stored value cards such as smart cards.

Co-ordination between Council Members

Australia's financial regulatory structure includes mechanisms to ensure effective co-ordination and co-operation between the three regulatory agencies. These mechanisms aim to provide full and timely exchange of information, the avoidance of duplication and a clear delineation of responsibilities, particularly when dealing with matters such as a financial disturbance.

The liaison framework, which is overseen by the Council itself, is a multi-tiered one. At the highest level is a structure of overlapping Board representation and regular senior meetings between the regulatory agencies. The legislation provides for both the RBA (two members) and ASIC (one member) to have representation on the APRA Board and for APRA (one member) to have representation on the Payments System Board. In addition, the APRA Board meets formally with the ASIC Commissioners at least once a year, and senior APRA and ASIC representatives meet every six months to discuss matters of mutual interest.

At the operational level, co-operation arrangements have been set out in three Memoranda of Understanding (MOUs) which have been signed between the RBA and APRA, between APRA and ASIC and, more recently, between the RBA and ASIC. The MOUs cover such matters as information sharing, prompt notification of any regulatory decisions likely to impact on the other agency's area of responsibility and consultation arrangements in the event of financial disturbances. The first two MOUs also establish bilateral Co-ordination Committees which aim, among other things, to avoid overlaps and gaps in regulatory coverage. Of course, at the broader level, this remains very much a focus of the Council.

The three MOUs are reproduced in Appendix B.

The value of co-operation between the regulatory agencies was highlighted by the events of September 11 in the United States, a matter which is discussed in the following Chapter. The agencies also co-operate on a range of more routine issues. One of these is the implementation of enhanced statistical reporting by Australian financial institutions. During the year, APRA completed the first phase of a major statistics project designed to improve financial data collections. This project has involved the

development of a new computer system to collect, analyse and store data from regulated entities and the introduction of new statistical reporting forms. The successful implementation of this project is fundamental to APRA's own responsibilities; it is also important for the provision of aggregate data to the RBA, in pursuit of its monetary policy and financial stability objectives, and to the production of economic data by the Australian Bureau of Statistics (ABS). As a result, both the RBA and the ABS were members of the steering group in the initial phase of the project and, along with APRA, now form a tripartite committee to provide ongoing co-operation on statistical issues.

The new computer system, known as Direct to APRA (D2A), provides a flexible, secure and user-friendly means of data collection. Following testing in mid 2001, the use of D2A was phased in from the September quarter, commencing with building societies and credit unions and with banks following in the first half of 2002. The forms will later be introduced in the insurance and superannuation sectors.

In designing its new reporting forms, APRA has sought to ensure that the information collected is relevant and useful to the needs of the respective agencies. Information collected for prudential purposes is intended, whenever possible and where prudential interests are not impaired, to reflect the way financial institutions themselves examine their businesses and to be consistent with accounting standards, rather than being a set of unique requirements. Because of their flexible design, the new reporting requirements can be changed to incorporate industry and international standards to make it easier for institutions to extract required data automatically from their own systems. In some cases, where industry practice diverges but use of the data for macroeconomic purposes requires consistency, standard definitions will be prescribed across all sectors. This will enable APRA to become the central repository of financial information on regulated entities, to which the RBA and ABS will have secure access when needed. Future requests for changes to reporting requirements will be dealt with in a predictable annual cycle, under the direction of the tripartite committee.

The year 2001 saw continued interaction between APRA and ASIC to achieve the appropriate level of regulatory co-operation. Both agencies aim, in particular, to co-ordinate actions while having due regard for their differing regulatory emphasis and practices. Liaison arrangements were reviewed in 2001 to better match organisational structures in each agency. Regular meetings are now held every two months on both a national and regional basis, with *ad hoc* meetings arranged to deal with specific operational matters as and when they arise.

Operational level liaison groups continue to focus on areas of common interest such as enforcement, compliance, disclosure and jointly regulated entities in the insurance and superannuation sectors. The agencies aim to share relevant findings of on-site reviews

and surveillance where such information could assist the other in carrying out its supervisory functions. A number of joint visits to financial institutions were conducted in 2001 as part of an APRA review of unit pricing in the superannuation industry.

A joint workshop between APRA and ASIC in March 2001 dealt with issues surrounding the licensing of superannuation and funds management entities regulated by both agencies. The workshop examined the different aims and methodology of each agency's supervisory processes and agreed to explore the scope to expand information sharing. A second joint enforcement workshop is planned in 2002 for frontline supervisors from both organisations.

ASIC and APRA are also committed to co-operating in the implementation of the FSR Act, particularly for those entities regulated by both agencies. Since late 2001, ASIC and APRA have held meetings specifically to deal with issues that arise during the transition period under the Act; their purpose is to share information on APRA-regulated licensees and to avoid duplication of responsibilities. Implementation of the FSR Act has also required liaison in other areas, such as the regulation of unauthorised foreign insurers and updates to superannuation audit requirements.

APRA and ASIC also consult in respect of business transfers under the *Financial Sector (Transfers of Business) Act 1999*.

In September 2001, the ASIC/APRA Enforcement Referrals Protocols were revised. The Protocols provide a summary of operational procedures for referral of existing, or anticipated, enforcement matters between APRA and ASIC. Regular meetings were held to discuss general enforcement issues, with case-specific liaison occurring as necessary. During the year, a joint task force between the two agencies was established in order to closely co-ordinate a particular enforcement action. This operation included the sharing of staff resources between the agencies.

3. MAJOR ISSUES FOR THE COUNCIL IN 2001

The Global Environment

Global economic conditions were particularly challenging for policy makers in 2001, with a marked slowdown in global growth, substantial adjustments in equity markets and other financial markets and severe financial shocks in the latter part of the year. The Council paid close attention to the impact of these developments on the stability of the Australian financial system.

The slowdown in global growth became evident around the start of 2001, in the wake of the collapse of the high-tech “bubble”, and it became more broad-based as the year proceeded. Economic forecasters progressively marked down their view of US and world growth prospects and there was an increasing realisation that Japan was again in recession. These developments were already in train prior to the events of September 11.

The terrorist attacks of September 11 sharply increased the risks to global financial stability, not only in the United States but around the world. The attacks themselves disrupted the normal operation of financial markets and impaired the trading capacity of financial institutions. Policy responses were prompt. In common with central banks in other major countries, the RBA sought to ensure, through its daily market operations, that uncertainty and heightened risk aversion did not lead to settlement problems or systemic failures in the Australian market. The RBA took steps to reassure participants that financial markets in Australia would function normally and that adequate liquidity would be available to meet their settlement needs. The RBA did not, however, see a case to depart from its normal timetable for considering monetary policy as a result of these developments. The key priority immediately following September 11 was to ensure that the financial system remained functional. The RBA liaised closely with APRA in the aftermath of the terrorist attacks, while APRA and ASIC also exchanged information in relation to specific institutions which appeared to be vulnerable. APRA subsequently issued a media release confirming that the Australian banking system clearly remained profitable and well-capitalised.

The terrorist attacks had an immediate impact on consumer and business confidence in the United States and elsewhere, reflected in a sharp fall in share prices and increases in risk measures such as credit spreads, but some of these impacts were short-lasting. The attacks have also led to the largest ever claims on the international insurance chain and cast doubt over the solvency of segments of the global insurance industry. Indications are that the overall direct exposure of Australian insurers is relatively small,

although a more lasting impact is likely to be an increase in global reinsurance premia and the withdrawal of terrorist cover by reinsurers.

In December, the major US energy company Enron filed for Chapter 11 bankruptcy protection. At first, the concern was that Enron could disrupt financial stability through the impact on its creditors or the unwinding of its large positions in financial markets. These fears have not been realised, mainly because exposures to Enron appear to have been widely dispersed. In Australia, a number of banks announced exposures to Enron, although these were small relative to the size of their overall loan portfolios. The more durable consequence of Enron's collapse is the increased scrutiny now being placed, in the United States and elsewhere, on accounting, disclosure and corporate governance standards.

The collapse of Enron was followed closely by the largest ever sovereign debt default when, after continuing economic and political turmoil, the government of Argentina defaulted on its debt and abandoned its decade-long currency board arrangements. Australia has very limited direct financial and trade linkages with Argentina, so the potential for the Argentine crisis to impair the health of the Australian financial system through these channels was considered minimal. Globally, there was only limited immediate contagion from Argentina to other emerging market economies, reducing the possibility of spillover effects in international financial markets.

In the face of the downturn of economic activity and this series of shocks, the prognosis for the world economy around the end of 2001 was a gloomy one, with fears of a prolonged and deep recession. Within a few months, however, a sense of optimism about global prospects began to reemerge on better news about the US economy, and international financial markets took on a generally more positive tone. Despite the difficult external environment in 2001, the Australian economy recorded a relatively strong performance which, in turn, helped to underpin the stability of the Australian financial system.

International Co-operation

Although international financial markets and core financial systems proved resilient to the unprecedented shocks of 2001, these shocks exposed issues that require attention from policy makers and confirmed the importance of maintaining the momentum of international monetary and regulatory reform. For one thing, the events of September 11 have renewed the focus on contingency planning and disaster recovery, to which much of the Year 2000 preparations had earlier been directed. For another, the collapse of Enron and other large corporate failures have highlighted the need to strengthen the basic foundations of markets through sound practices of corporate governance,

improved audit quality and more effective regulatory oversight. Council members participate in a wide range of international groupings dealing with these and other reform issues. The Council itself acts as a forum for sharing information and co-ordinating the participation of its members in these activities.

One of the key groupings is the Financial Stability Forum, which was established in 1999. The Forum provides for the regular exchange of high-level views on potential vulnerabilities in the international financial system and helps to prioritise the various reform efforts that are underway at any one time. It brings together national authorities responsible for financial stability in significant financial centres, international financial institutions, sector-specific international groupings of regulators and supervisors, and committees of central bank experts. The Governor of the RBA represents Australia.

During 2001, the Forum – which held its first Asia-Pacific Regional Meeting in Tokyo in October – also reviewed progress in addressing some of its earlier concerns about vulnerabilities in the international financial system, particularly lax regulatory practices in some offshore financial centres (OFCs) and the activities of highly leveraged institutions (HLIs). The Forum noted that some OFCs had made good progress in implementing international standards of supervision and regulation, though others were lagging behind. Further steps to encourage compliance will be considered once the International Monetary Fund (IMF) has completed an assessment program of OFCs. The Forum was also generally encouraged by changes in the industry and market environment for HLIs. Improved counterparty risk management and strengthened regulatory oversight of HLI counterparties appear to have reduced the leverage of HLIs from previous peaks; in addition, HLIs are now generally smaller in size. These developments have lessened the risks that HLIs could pose for the international financial system. However, the Forum has warned against complacency and urged continued improvements on public disclosures by HLIs to strengthen market discipline and reduce systemic risk.

The Forum has also been seeking to reinforce international crisis management arrangements, in particular, the practical issues associated with the winding down of a large and complex financial institution. A Crisis Management Contact List has been established, covering central banks, supervisory/regulatory agencies, finance or treasury departments, key international financial institutions, and global service providers in some 30 countries, including Australia.

A second international grouping with which Australia is associated is the G20, which was also established in 1999. The G20 brings together representatives of a cross-section of systemically significant economies, and of the IMF and World Bank; the aim is to

promote co-operation so as to achieve stable and sustainable world economic growth.³ The Ministerial meeting, attended by the Treasurer and the Governor of the RBA, is held annually while Deputies' meetings are held twice-yearly.

The primary focus of the G20 has been on ways to reduce the frequency and severity of financial crises. In November 2001, the Ministers and Governors reaffirmed their commitment to efforts to reduce susceptibility to financial crises through their work in four key areas: the selection of appropriate exchange rate arrangements; prudent management of external liabilities; implementation of international standards and codes of best practice; and the development of a workable framework for involving the private sector in crisis prevention and resolution. The G20's agenda also includes consideration of the challenges posed by globalisation. Ministers and Governors have agreed on the importance of developing policies to ensure that the benefits of globalisation are maximised and shared by developing and poor countries. Members have undertaken case studies reviewing experiences with globalisation to provide a foundation for an appropriate policy framework. Building on this work, the RBA and the Australian Treasury jointly convened a conference on "Globalisation, Living Standards and Inequality: Recent Progress and Continuing Challenges" in Sydney in May 2002.

The G20 responded to the emergence of terrorism as a threat to international financial stability by committing to an Action Plan to deny terrorists and their associates access to financial systems; the RBA has taken action to work towards these aims. The G20 has urged countries outside the grouping to take similar steps.

ASIC, principally through its membership of the International Organisation of Securities Commissions (IOSCO), as well as through its regional training and bilateral enforcement activities, plays an active role in international co-operation efforts in financial market regulation. Following the events of September 11, ASIC became a member of the IOSCO September 11 Taskforce, which was established to explore actions that securities regulators should take in light of those events. ASIC was also involved in regular IOSCO activities throughout the year including attendance at meetings of the IOSCO Implementation Committee, which reviews progress in the implementation of IOSCO principles in the Asia-Pacific region. Along with 41 other IOSCO members, ASIC took part in the IOSCO-sponsored International Internet Surf Day aimed at increasing investor protection and market confidence.

One particular area in which ASIC was involved during 2001 concerned cold-calling. Cold-calling is the practice whereby an unlicensed person makes unsolicited telephone offers urging unsuspecting investors to buy securities in overseas stocks. In June 2001,

3 Members comprise the G7 countries as well as Argentina, Australia, Brazil, China, India, Indonesia, Mexico, Russia, Saudi Arabia, South Africa, South Korea, Turkey and the European Union.

ASIC presented a proposal at the IOSCO annual meeting that Asia-Pacific Regional Committee (APRC) members agree to work towards developing a regional cold-calling communications strategy. That proposal was adopted, and ASIC subsequently canvassed all APRC members on any enforcement actions or consumer protection measures they had taken in relation to cold-calling. In October 2001, at the IOSCO Technical Committee meeting in Rome, ASIC presented a briefing paper which it had prepared with the Securities Exchange Board of India, as well as a general communiqué drawing attention to the dangers for investors of investing through a cold-caller; the communiqué was issued in February 2002. At the same time, ASIC worked closely with Hong Kong enforcement officials, and with Thai police investigating various cold-calling firms operating from Thailand which had been sent money by Australian investors.

During 2001, ASIC hosted numerous visits from regional regulatory staff and continued to provide training and assistance. A number of senior ASIC officers gave presentations at various regional seminars, including a conference on financial service reform hosted by the Asia-Pacific Economic Cooperation (APEC) in Beijing in November 2001. During the year, ASIC also negotiated MOUs with regulatory counterparts overseas – the Comissão Nacional de Valores Mobiliários of Portugal, the Capital Markets Board of Turkey, the Hong Kong Securities and Futures Commission and the Commodity Futures and Trading Agency of Indonesia.

APRA was also active in a range of international groupings throughout 2001 and views international co-ordination and co-operation as an important aspect of its work. APRA is represented on, and provides input to, a range of groups established under the auspices of the Basel Committee on Banking Supervision. These include the Core Principles Liaison Group (CPLG), the main forum for consultation between the Basel Committee, which largely comprises central banks and bank supervisory agencies from G10 countries, and non-member countries. APRA plays an active role on the CPLG Capital Working Group, which provides advice and guidance on the development of the new Basel Capital Accord. APRA was a member of a separate Task Force established by the Financial Stability Forum and the Basel Committee to produce a “tool kit” containing guidance for supervisors when dealing with weak banks. The Task Force’s report, which was released in March 2002, assesses various methods of dealing with bank problems, including preventative measures, early identification, corrective actions, resolution issues and exit strategies. APRA is also represented on the Basel Committee’s Electronic Banking Group, which examines the prudential issues arising from electronic banking activities and, in particular, develops guidance for supervisors in dealing with the specific risk management and cross-border issues that e-banking presents.

APRA is represented on the Executive Committee of the International Association of Insurance Supervisors (IAIS), where an APRA executive is currently Deputy Chair;

during 2001, it provided the Chair of the IAIS Solvency Sub-Committee, which is developing international guidance on the establishment of solvency standards for life and general insurance companies. APRA is also a member of the Joint Forum, established by the IAIS, the Basel Committee and IOSCO to examine cross-sector issues. The Joint Forum produced two major discussion papers in 2001: one on the similarities and differences in the Core Principles for the respective sectors and another which examined the different approaches to risk assessment and capital adequacy adopted within the banking, insurance and securities industries.

During 2001, the International Network of Pensions Regulators and Supervisors was established. Given APRA's responsibilities with respect to Australia's well-developed superannuation sector, APRA has taken considerable interest in the establishment of this new grouping and is a member of its technical committee.

Together with the RBA, APRA participates in the Working Group on Banking Supervision of the Executives' Meeting of East Asia-Pacific Central Banks (EMEAP), a grouping of regional central banks and monetary authorities. The Working Group provides a forum to discuss financial developments in the region as well as progress on the new Basel Capital Accord.

Finally, APRA and ASIC have been active supporters of the APEC Financial Regulators Training Initiative. During 2001, APRA hosted a course for APEC banking supervisors on corporate governance and internal controls. The objective of such courses is to ensure a strong transfer of knowledge to countries within the region who are seeking to upgrade their regulatory systems, by drawing on the skills and expertise of other supervisors.

APPENDIX A

COUNCIL MEMBERSHIP

Organisation Office	Representation	Internet Address	Information
Reserve Bank of Australia	Mr IJ Macfarlane (Chairman) Governor Dr JF Laker Assistant Governor (Financial System)	www.rba.gov.au	(02) 9551 9721
Australian Prudential Regulation Authority	Mr GJ Thompson Chief Executive Officer Mr WS Byres General Manager Policy, Research and Consulting	www.apra.gov.au	(02) 9210 3000
Australian Securities and Investments Commission	Mr DW Knott Chairman Mr G Tanzer Executive Director of International Affairs	www.asic.gov.au	(02) 9911 2600

Administrative Arrangements

The Council of Financial Regulators does not have its own staff; support is provided by RBA officers. The Council met three times in 2001, and aims to meet on a quarterly basis each year.

The production and printing costs of this Annual Report were met by the RBA; distribution costs were shared by the members.

The Federal Treasurer has Ministerial responsibility for the Council. Although there is no statutory requirement for the Council to table its report in Federal Parliament, the Treasurer has agreed to do so on this occasion.

APPENDIX B

MEMORANDA OF UNDERSTANDING BETWEEN COUNCIL MEMBERS

THE RESERVE BANK OF AUSTRALIA AND THE AUSTRALIAN PRUDENTIAL REGULATION AUTHORITY

Objective

1. This Memorandum of Understanding sets out a framework for co-operation between the Reserve Bank of Australia (RBA) and the Australian Prudential Regulation Authority (APRA) which is aimed at promoting the stability of the Australian financial system.

Responsibilities

2. The responsibilities of the RBA and APRA for promoting financial stability are largely complementary.
3. The RBA's role is focused on the objectives of monetary policy, overall financial system stability and regulation of the payments system. It has no obligation to protect the interests of bank depositors and will not supervise any individual financial institutions. The RBA does, however, have discretion to provide emergency liquidity support to the financial system.
4. APRA is responsible for the prudential supervision of banks, life and general insurance companies and superannuation funds. Supervision of building societies, credit unions and friendly societies will transfer to APRA from State jurisdictions at a later date. APRA has powers to act decisively in the interests of depositors or policy holders and fund members if a supervised institution is in difficulty.

Sharing of Information

5. Full and timely exchange of information is a crucial element in co-ordination between the RBA and APRA.
6. The RBA gathers data and other information through its participation in financial

markets and its pivotal role in the payments settlement system. APRA gathers a wide range of prudential data on the institutions which it supervises.

7. The RBA and APRA agree that, subject to legislative provisions, information available to one which is relevant to the responsibilities of the other will be shared as requested. Each organisation will provide relevant information to the other on a best endeavours basis, with due regard to the urgency of doing so.
8. When exchanging confidential information, the RBA and APRA acknowledge the confidentiality and secrecy requirements of the Acts under which they operate. Each organisation has the right to specify the level of confidentiality attached to information provided to the other.
9. The RBA and APRA will work together to avoid duplication in the collection of information so as to minimise the reporting burden on financial institutions. Subject to appropriate cost sharing, the RBA may arrange for information relevant to its responsibilities to be collected from financial institutions by APRA.
10. APRA will be responsible for the custody of all records relating to the supervision of banks, including those records transferred to APRA on its establishment. It will ensure that, subject to legislative provisions, the RBA has free and open access to these records.

Threats to Financial System Stability

11. If either the RBA or APRA identifies a situation which it considers is likely to threaten the stability of the financial system, it will inform the other as a matter of urgency. Responses to a disturbance of this type will depend on the particular circumstances prevailing, but in all cases the RBA and APRA will keep each other informed of their ongoing assessment and will consult closely on proposed actions.
12. The RBA will be responsible for determining whether, and how, it might provide emergency liquidity support to the financial system. It does not see its balance sheet as available to support the solvency of an individual financial institution in difficulty.

RBA Participation in Prudential Consultations

13. To assist it in keeping abreast of financial developments and supervisory issues, the RBA will participate from time to time in APRA's regular on-site reviews of, and prudential consultations with, supervised institutions. The RBA will give APRA appropriate notice of its intention to participate in such reviews/consultations.

Consultation on Regulatory Policy Changes

14. Each organisation will notify the other of any proposed changes in regulatory policy, and provide the opportunity to consult on changes which are likely to impinge on the responsibilities of the other.

International Representation

15. The RBA and APRA will co-operate closely to ensure that Australia has appropriate representation in regional and international supervisory fora and training initiatives. In some circumstances there will be joint representation; for example, APRA will join the RBA in the relevant study groups of the Executive Meeting of East Asia and Pacific (EMEAP) central banks. In other circumstances only one institution will be represented; for example, APRA has assumed the RBA's membership of the Core Principles Liaison Group in the Basle Committee on Banking Supervision. In the latter cases, the two organisations will consult with each other as needed before and after the particular gathering.

Co-ordination Committee

16. A joint Co-ordination Committee will be established to facilitate close co-operation between the RBA and APRA. The Committee will be responsible for ensuring that appropriate arrangements are in place to respond to threats to system stability, and for co-ordinating information sharing. It will also handle operational matters such as statistical collections, joint research work and participation in international fora.
17. The Committee will be chaired by the Assistant Governor (Financial System) of the RBA and meet monthly or more frequently as required.

I.J. Macfarlane

Governor

Reserve Bank of Australia

G.J. Thompson

Chief Executive Officer

Australian Prudential

Regulation Authority

SYDNEY

12 October 1998

THE AUSTRALIAN PRUDENTIAL REGULATION AUTHORITY AND THE AUSTRALIAN SECURITIES AND INVESTMENTS COMMISSION

1. Objective

- 1.1 This memorandum of understanding (MOU) sets out a framework for co-operation between the Australian Prudential Regulation Authority (APRA) and the Australian Securities and Investments Commission (ASIC) (the agencies) in areas of common interest where co-operation is essential for the effective and efficient performance of their respective financial regulation functions.
- 1.2 The agencies agree that consistent with their separate roles they will co-operate where it is within their administrative powers to reduce duplication and compliance costs and achieve effective enforcement and compliance outcomes.
- 1.3 This MOU is not intended to create binding obligations on either agency and each agency has the right to vary its terms at any time by agreement following consultation with the other agency.

2. Responsibilities

- 2.1 APRA is responsible for the prudential supervision for banks, life and general insurance companies and superannuation funds. If the State and territory Governments agree, APRA will also be responsible for the prudential supervision of building societies, credit unions and friendly societies. In performing its functions to protect the interest of depositors, policyholders and fund members APRA is required to balance financial safety with efficiency, competition, contestability and competitive neutrality.
- 2.2 ASIC is responsible for the administration and enforcement of the national scheme laws, being laws of the Commonwealth and the States in relation to Australian companies, securities, managed investments and futures markets; and for monitoring and promoting market integrity and consumer protection in relation to the Australian financial system, the provision of financial services and the payment system.

3. Regulatory Policy Development

- 3.1 Changes in regulatory policy or regulatory decisions on particular matters by either agency may have implications for the other agency. Each agency therefore will notify the other of any proposed changes in regulatory policy or regulatory decisions likely to impact on the responsibilities of the other and provide the other with the opportunity to comment on any proposed changes.
- 3.2 Where implementation of regulatory policy or regulatory decisions by either agency has implications for the other agency, each agency will notify the other where such implementation is likely to impact on the responsibilities of the other.
- 3.3 The agencies agree that, where appropriate, it is desirable for them to consult with each other in relation to policy statements and media releases, which are being formulated and which may be of interest to or have an effect on each agency. Where appropriate, the agencies may consider whether to issue a policy statement or media release on a joint basis, having regard to the subject matter of the release, the policy objectives of each regulator, and the objectives of this agreement.

4. Mutual Assistance

- 4.1 The agencies recognise that it is important that they co-operate to promote confidence in the financial system and the confident and informed participation of all stakeholders in that system.
- 4.2. The agencies agree to provide each other with mutual assistance in relation to the exchange of information, appropriate referral of matters and co-operation in regulation, compliance, and enforcement within the framework of this agreement and which is consistent with all relevant laws.

5. Co-ordination Committee

- 5.1 A joint Co-ordination Committee will be established to facilitate close co-operation between APRA and ASIC. The Committee will operate according to a Charter and be responsible for ensuring the appropriate arrangements are in place for matters such as co-ordinating information-sharing, joint inspections or task forces, referral of cases and enforcement action or major supervisory intervention. It will also co-ordinate operational matters such as administrative arrangements to avoid duplication, statistical collections, joint research work or training or industry consultation, and participation in international fora.

- 5.2 It is envisaged that liaison in respect of routine operational matters will occur on an ‘as needed’ basis between appropriate staff of the two agencies.

6. Information-Sharing

- 6.1 Full and timely exchange of information is a crucial element in co-ordination between APRA and ASIC.
- 6.2 APRA gathers a wide range of information on the entities, which it prudentially supervises. ASIC gathers a wide range of information in its role in monitoring and promoting market integrity and consumer protection in relation to the Australian financial system.
- 6.3 The agencies agree that, subject to legislative provisions, information available to one agency, which is relevant to the responsibilities of the other agency, will be shared as requested. Each agency will provide relevant information to the other on a best endeavours basis, with due regard to the urgency of doing so. This will be subject to any relevant legal and operational considerations and any conditions, which the provider of the information might place upon the use or disclosure of the information, such as claims of legal professional privilege.
- 6.4 When exchanging confidential information, APRA and ASIC acknowledge the confidentiality and secrecy requirements of the Acts under which each agency operates. The agency providing information has the right to specify the level of confidentiality attached to the information it provides to the other, in order to protect that information from unauthorised use, or disclosure. The agency receiving the information will take all reasonable steps to ensure such information is only used or disclosed for the purpose for which it was obtained.
- 6.5 Each agency agrees not to disclose any confidential information obtained pursuant to this agreement to a third party unless it has obtained the prior consent of the agency which has provided the confidential information.
- 6.6 Subject to appropriate cost sharing, each agency may arrange for information relevant to its responsibilities to be collected from financial entities by the other agency.

7. Unsolicited Assistance

- 7.1 Each agency recognises that in the course of carrying out its functions and exercising its powers, it will come into possession of information which would, if provided to the other agency, be likely to assist that other agency in administering or enforcing the particular laws for which it is responsible.

7.2 Each agency agrees, subject to legal restrictions, to use its best endeavours to notify the other agency with due regard to the urgency of doing so of the existence of any information of a kind referred to above, notwithstanding that it may not have received a request from the other agency for such information.

8. Cost of Provision of Information

8.1 In general, the agency which receives the request for information shall bear the cost incurred by it in locating and providing the information to the agency who requests the information.

8.2 If it appears to the agency that receives the request that it will incur substantial costs in responding to the request it may make representations to that effect to the requesting agency and the parties may negotiate a cost-sharing arrangement in relation to the provision of that information.

9. International Representation

9.1 The agencies will co-operate to ensure that Australia has appropriate representation in regional and international regulatory fora and training initiatives. In some circumstances there will be joint representation but where only one agency is represented it will consult with the other agency as needed before and after the particular gathering.

DATED this day 12 of October 1998

ALAN CAMERON AM

Chairman
Australian Securities and
Investments Commission

GRAEME THOMPSON

Chief Executive Officer
Australian Prudential Regulation
Authority

THE AUSTRALIAN SECURITIES AND INVESTMENTS COMMISSION AND THE RESERVE BANK OF AUSTRALIA

Objective

1. This Memorandum of Understanding between the Australian Securities and Investments Commission (ASIC) and the Reserve Bank of Australia (RBA) is intended to assist each agency in the performance of its regulatory responsibilities under the *Corporations Act 2001* in relation to clearing and settlement facilities.
2. The framework set out in this Memorandum of Understanding is also intended to promote transparency, help prevent unnecessary duplication of effort and minimise the regulatory burden on licensed facilities.

Responsibilities

3. The RBA has specific responsibilities under the *Corporations Act 2001* for setting financial stability standards, monitoring compliance with these standards and ensuring that licensed clearing and settlement facilities do all things reasonably practicable to reduce systemic risk.
4. ASIC has responsibility under the *Corporations Act 2001* for monitoring compliance with all other legislative obligations imposed on licensed clearing and settlement facilities. These include a requirement to provide financial services in a fair and effective manner, including by having arrangements in place to enforce compliance with operating rules and for resolving complaints from facility participants.
5. ASIC also has responsibility under the *Corporations Act 2001* for taking action to enforce compliance with all obligations imposed upon licensed clearing and settlement facilities.

Consultation

6. To promote effective and well-coordinated development of regulatory policy, ASIC and the RBA will inform each other when determining substantive issues of policy with respect to clearing and settlement facilities which may have an impact on the regulatory responsibilities of the other agency. Each will provide the other with the opportunity for consultation on the proposed policy prior to any public consultation period, and prior to the release of a finalised policy.

Formal Requests and Use of Powers

7. Where either ASIC or the RBA proposes to formally exercise any of its powers relating to licensed clearing and settlement facilities under the *Corporations Act 2001*, and this exercise may have an impact on the regulatory responsibilities of the other agency, it will:
 - notify the other agency of the proposed use of powers;
 - consult with the other agency on the proposed use of powers;
 - notify the other agency when the power is formally exercised; and
 - subject to any restrictions imposed by law, provide to the other agency any relevant documentation.
8. Under section 823E of the Act, ASIC may give a direction to a licensed clearing and settlement facility to take specific measures to comply with a financial stability standard or to take any other action to reduce systemic risk. It may do this on its own initiative, or following a request from the RBA.
9. ASIC anticipates that it would generally take such action at the request of the RBA, which has responsibility for assessing licensees' compliance with financial stability standards and their obligation to do all things reasonably practicable to reduce systemic risk.
10. ASIC and the RBA will agree on detailed protocols for the handling of requests under section 823E of the Act and exchanges of information in relation to any formal exercise of power.

Notification and Information Sharing

11. There are circumstances where ASIC or the RBA will receive or make notifications that are required under the Act. Subject to any restrictions imposed by law, ASIC and the RBA will inform each other of any notifications either makes or receives with respect to clearing and settlement facilities which may have an impact on the regulatory responsibilities of the other agency.
12. In addition to the exercise of formal powers and requests ASIC and the RBA will (subject to any restrictions imposed by law) share information that they believe would be of assistance to the other in undertaking its responsibilities under the Act.
13. Wherever possible, ASIC and the RBA will avoid separate collection of the same information and data from licensed clearing and settlement facilities.

14. Where ASIC or the RBA has been served with a compulsory notice which would require the disclosure to some third party of information obtained under this MOU, the agency will, prior to disclosure, notify the other agency in writing so as to enable the other agency to determine what action, if any, it should take.

Report to the Minister on Annual Assessment

15. Both ASIC and the RBA are required under the *Corporations Act 2001* to conduct an annual assessment of each clearing and settlement facility licensee's compliance with particular obligations under the Act and to prepare a report to the Minister on that assessment. Under the *Corporations Act 2001*, each agency is required to give a copy of that report to the other agency. Where such a report raises issues that may have an impact on the regulatory responsibilities of the other agency, each agency will provide for appropriate consultation with the other agency prior to finalisation of the report.

Coordination Meetings and Liaison

16. ASIC and the RBA will establish procedures to facilitate regular contact between officers of the organisations on routine operational matters.
17. ASIC and the RBA will hold meetings of senior officials at least every twelve months to discuss the coordination of matters relevant to the regulation of clearing and settlement facilities and the operation of this MOU.

DATED this day 18 March 2002

D Knott
Chairman
Australian Securities and
Investments Commission

IJ Macfarlane
Governor and Chairman
Payments System Board
Reserve Bank of Australia

APPENDIX C

MAIN TYPES OF FINANCIAL INSTITUTIONS as at December 2001

Type of Institution	Main Supervisor/ Regulator	Main Characteristics	No. of Active Groups ^a	Total Assets (\$b)
Banks	APRA	Provide a wide range of financial services to all sectors of the economy, including (through subsidiaries) funds management and insurance services. Foreign banks authorised to operate as branches in Australia are required to confine their deposit-taking activities to wholesale markets.	52	835 ^b
Non-bank financial intermediaries				
Building societies	APRA	Building societies raise funds primarily by accepting deposits from households, provide loans (mainly mortgage finance for owner-occupied housing) and payments services. Traditionally mutually owned institutions, building societies increasingly are issuing share capital.	17	12
Credit unions	APRA	Mutually owned institutions, credit unions provide deposit, personal/housing loan, and payment services to members.	201	25
Money market corporations ('merchant banks')	ASIC ^c	Operate primarily in wholesale markets, borrowing from, and lending to, large corporations and government agencies. Other services, including advisory, relate to corporate finance, capital markets, foreign exchange and investment management.	40 ^d	86
Finance companies (including general financiers)	ASIC ^c	Provide loans to households and small-to medium-sized businesses. Finance companies raise funds from wholesale markets and, using debentures and unsecured notes, from retail investors.	73 ^d	88
Securitisers		Special purpose vehicles that issue securities backed by pools of assets (eg mortgage-based housing loans). The securities are usually credit enhanced (eg through use of guarantees from third parties).	113	97

Type of Institution	Main Supervisor/ Regulator	Main Characteristics	No. of Active Groups ^a	Total Assets (\$b)
Funds managers and insurers				
Life insurance companies	APRA ^e	Provide life, accident and disability insurance, annuities, investment and superannuation products. Assets are managed in statutory funds on a fiduciary basis, and are mostly invested in equities and debt securities.	33	188
Superannuation and approved deposit funds (ADFs)	APRA	Superannuation funds accept and manage contributions from employers (incl. self-employed) and/or employees to provide retirement income benefits. Funds are controlled by trustees, who often use professional funds managers/advisers. ADFs are generally managed by professional funds managers and, as with super funds, may accept superannuation lump sums and eligible redundancy payments when a person resigns, retires or is retrenched. Superannuation funds and ADFs usually invest in a range of assets (equities, property, debt securities, deposits).	11 072 ^f	331
Management companies (public unit trusts)	ASIC ^c	Unit trusts pool investors' funds, usually into specific types of assets (eg equities, property, money market investments, mortgages, overseas securities). Most unit trusts are managed by subsidiaries of banks, insurance companies or merchant banks.	97	152
Trustee companies (common funds)	State authorities	Trustee companies pool into common funds money received from the general public, or held on behalf of estates or under powers of attorney. Funds are usually invested in specific types of assets (eg money market investments, equities, mortgages).	13	8
Friendly societies	APRA	Mutually owned co-operative financial institutions offering benefits to members through a trust-like structure. Benefits include investment products through insurance or education bonds; health; funeral; accident; sickness; or other benefits.	38	6
General insurance companies	APRA ^e	Provide insurance for property, motor vehicles, employers' liability, etc. Assets are invested mainly in deposits and loans, government securities and equities.	97	64

a Subsidiaries of an institution undertaking the same activity are treated as part of a single group.

b Refers only to the Australian banking operations and does not include assets of banks' overseas branches or domestic and foreign non-bank subsidiaries. Banks' global consolidated group assets (for all locally incorporated and foreign bank branches) at December 2001 were \$1130 billion.

c ASIC does not conduct prudential supervision of these institutions, but does regulate certain aspects of their operations (eg compliance with the fundraising and securities licensing provisions of the Corporations Law).

d As from December 1999, groups with total assets below \$50 million are not included.

e State Government-owned insurance offices are not covered by Commonwealth legislation, nor supervised by APRA.

f Includes assets in life office statutory funds, but excludes pooled superannuation trusts, non-regulated public sector funds and self-managed superannuation funds (which have less than five members); self-managed funds are regulated by the Australian Taxation Office. Total superannuation assets were estimated to be around \$528 billion as at December 2001.

APPENDIX D

MAIN DEVELOPMENTS IN REGULATION/SUPERVISION OF THE AUSTRALIAN FINANCIAL SYSTEM: 2001

Jan The Basel Committee on Banking Supervision releases a revised and more extensive consultative paper on reform of capital adequacy guidelines for banks. APRA immediately welcomes the proposals as giving depositors better protection against the risks in banking and being flexible enough to apply to a wide range of authorised deposit-taking institutions.

ASIC requests 53 “new economy” companies, which operate in high-tech, dot com or related business sectors, to clarify their financial reporting and disclosure following surveillance of the financial reports and cash flow statements of a larger number of such companies.

Feb ASIC announces tighter guidelines governing financial forecasts and projections in prospectuses, in response to concerns about unreasonable and non-verifiable financial projections based on hypothetical assumptions. This followed a regulatory review of prospectuses issued in 2000.

ASIC announces a major investigation into the financial status of Australia’s unlisted solicitors’ mortgage investment schemes. The investigation is designed to identify the best steps available to minimise investor loss as well as issues of negligence and misconduct.

ASIC commences a formal investigation into the market disclosure of HIH Insurance Ltd, following concerns that the market was being inadequately informed about the company’s trading position. The investigation places particular emphasis on corporate governance, market disclosure and possible insolvent trading.

ASIC announces the results of a campaign that has significantly improved compliance by investment advisers with a fundamental “consumer protection” condition of their licence. In response to ASIC’s campaign, a total of 419 advisers will join an approved consumer complaints resolution scheme, known as the Financial Industry Complaints Service (FICS).

ASIC carries out a campaign to examine how life insurance companies train and supervise agents in disability insurance products and looks at the conduct and disclosure of those agents when advising on such products.

- APRA launches its new quarterly statistical publication, *Insight*, aimed at giving readers insight into the condition of Australia’s financial institutions and APRA’s supervision. The tables and graphs within *Insight* focus primarily on the financial and risk characteristics – or prudential soundness – of APRA-supervised financial institutions. They emphasise comparisons across institutions, rather than time trends in industry aggregates.
- Mar ASIC launches an electronic bulletin that will provide updates on investments, superannuation, insurance and on how to avoid the latest financial scams.
- APRA releases further proposals to reform and modernise the prudential supervision of general insurance companies in Australia, updated from earlier draft proposals released in 2000. (In November 2000, the Government had announced that it would be proceeding with amendments to the *Insurance Act 1973* necessary to give effect to the new regime.)
- Apr Following a decision by the Payments System Board, the RBA “designates” credit card schemes operated in Australia by Bankcard, MasterCard and VISA, as payment systems subject to its regulation under the *Payment Systems (Regulation) Act 1998*.
- ASIC launches a draft “Guide to Good Transaction Fee Disclosure for Banks, Building Societies and Credit Unions”, which sets out ASIC’s views on disclosure of product selection fees, fee changes, when fees are charged, when a statement is received and fees charged before providing a statement.
- ASIC commences investigation into certain issues of market disclosure and governance by NRMA Insurance Group Limited and NRMA Limited.
- ASIC launches a revised Electronic Funds Transfer (EFT) Code of Conduct. The revised code is extended to include telephone and internet banking, all credit card transactions (other than those intended to be authenticated by a manual signature) and stored value products such as smart cards, pre-paid telephone cards and digital cash.
- APRA announces plans to review the *Life Insurance Act 1995*. This review also seeks to harmonise and integrate the prudential requirements of friendly societies within this Act.
- APRA releases its self-assessment of the prudential supervision of Australian banks against the Basel Committee’s Core Principles for Effective Banking Supervision.
- May ASIC announces how it will facilitate the use of electronic applications in the life insurance and superannuation industries.

The Government reiterates its intention to proceed with the legislative changes needed for implementation of APRA's new prudential supervision framework for general insurance companies, and announces a new (shorter) implementation timetable. APRA hosts an industry seminar to discuss its proposed new framework.

The Government announces a Royal Commission into the collapse of HIH Insurance Group, as well as a package of assistance for policyholders of HIH facing financial hardship.

Jun ASIC releases a second package of policy proposal papers arising from the Financial Services Reform Bill 2001, relating to licensing and approval of codes. APRA releases its submission on the Basel Committee's consultative paper on proposed changes to the Basel Capital Accord.

APRA releases its submission to the Productivity Commission's National Competition Policy review of the *Superannuation Industry (Supervision) Act 1993* and certain other superannuation legislation. The submission outlines key areas where APRA plans to strengthen supervision within the current legislative structure including better information provided to APRA; stricter guidelines on funds' investment portfolios; wider powers for APRA to seek information directly from third-party service providers; reassessment of minimum capital requirements in superannuation; and broader licensing arrangements.

Jul Following ASIC representations, the Securities and Exchange Commission of Thailand launches a crackdown on alleged cold-callers in Bangkok.

APRA and the Australian Taxation Office jointly issue a circular directed at employers that explains their obligation to send employees' voluntary superannuation contributions promptly to the nominated superannuation fund.

Aug Parliament passes the *Financial Services Reform Act 2001* (FSR Act).

Parliament passes amendments to the *Insurance Act 1973* to give effect to APRA's new prudential supervision framework for general insurance.

APRA releases for industry comment a draft prudential standard on Board composition for all ADIs.

Sep ASIC releases an FSR Act policy proposal paper on licensing and financial requirements.

ASIC issues a notice to unlisted fund managers which, as a result of the events of September 11, suspended applications and redemptions. The notice reminds managers of their obligations to consider the best interests of scheme investors.

Oct The RBA takes action under the *Banking (Foreign Exchange) Regulations* to block any accounts that might exist in the name of persons or organisations identified by the United Nations and the United States as terrorists or their sponsors.

ASIC releases two guides to assist the industry in making the transition to the new FSR Act regime. “Licensing and disclosure: making the transition” explains how the transitional provisions for financial services licensing and product disclosure work and “How do you get an Australian financial services licence?” explains the ASIC licensing process and the types of licence for which applications can be made.

The Government releases an Issues Paper on “Options for Improving the Safety of Superannuation.”

APRA releases a Policy Discussion Paper on two aspects of its framework for the prudential supervision of conglomerate groups that include an ADI – large exposure limits (both intra-group and external) and the measurement of capital adequacy in conglomerate groups.

APRA begins a campaign to remind superannuation trustees of their obligation to lodge annual returns on time, and of the consequences of late lodgement.

Nov ASIC issues six policy statements and one guidance paper on licensing and disclosure matters to assist the industry in understanding the implementation of the FSR Act.

APRA releases the latest versions of its proposed new prudential standards for general insurance companies in Australia. The standards cover capital adequacy, liability valuation, reinsurance arrangements, risk management, assets in Australia and transfers of business.

Reflecting the growing importance of outsourcing in the financial sector, APRA releases for comment a draft prudential standard on outsourcing by ADIs. The draft standard aims to ensure that the Board and management of ADIs have policies and procedures to manage effectively the risks arising from outsourcing business activities.

Dec The RBA releases for public discussion a consultation document on reform of credit card schemes in Australia, proposing standards and an access regime that will promote greater efficiency, transparency and competition in the Australian payments system.

ASIC announces a project to look at disclosure of fees and charges in the product disclosure statements for investment products.

ASIC releases a policy statement that deals with financial resource requirements for financial service providers.

APRA releases for comment four draft revised prudential standards (including their related guidance notes) for ADIs. These standards give effect to the policy framework for prudential supervision of conglomerate groups containing ADIs described in the April 2000 Policy Information Paper and the October 2001 Policy Discussion Paper.

APPENDIX E

SPEECHES AND ARTICLES OF COUNCIL MEMBERS

Copies of the following speeches and articles are published on the Internet site or available from the Information Office of the relevant agency – see page 22.

Australian Prudential Regulation Authority

Thompson, G.J., *On APRA's Plate*, National Council Dinner of the Trustee Corporations Association of Australia, 26 March 2001.

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