

# INTRODUCTION

## Background to the inquiry

- 1.1 In March 1997, the Financial Systems Inquiry, commonly known as the Wallis Committee, recommended a reorganisation of the Australian financial services regulatory framework. Part of the recommended reorganisation was the formation of a single prudential regulator for the financial services sector.<sup>1</sup>
- 1.2 As part of the implementation of the Wallis Committee recommendations, the Australian Prudential Regulatory Authority (APRA) became fully operational on 1 July 1998.<sup>2</sup>
- 1.3 APRA describes its purpose as the:

... prudential regulation of Australia's financial institutions. This means we promote business behaviour by deposit takers, insurers and superannuation funds to maximise the likelihood that they will remain in a sound financial condition so that they can meet their repayment obligations to depositors, policy holders or fund members, as the case may be...<sup>3</sup>
- 1.4 APRA has been provided with comprehensive powers in its area of responsibility, including the licensing of financial institutions, and making

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1 Financial Systems Inquiry. *Financial Systems Inquiry Final Report*. 1997. Melbourne, FSI, pp 312-317.

2 Department of the Treasury. 'Reform Of The Australian Financial System.' *Economic Round-Up*, Winter 1998. Canberra, AGPS, p 19.

3 Evidence p 2.

standards on prudential matters in relation to Authorised Deposit Taking Institutions (ADIs), superannuation funds, and insurance companies.<sup>4</sup>

1.5 It is also useful to clarify what APRA is not responsible for. During the 4 September 2000 hearing, APRA indicated:

...We are not responsible for policing competition in financial markets, for standards of disclosure about products and services or for how banks and others handle customer complaints and disputes. We are not responsible for fees, charges or interest margins, or for the representation of financial institutions in particular regional areas.

1.6 APRA is funded by levies paid by regulated financial institutions and is accountable through an independent board. To ensure there is a close relationship between the Reserve Bank of Australia (RBA), the Australian Securities and Investments Commission (ASIC), and APRA, the RBA has two representatives and ASIC one representative on the APRA board.<sup>5</sup>

1.7 APRA is split into three divisions: the Diversified Institutions Division; the Policy, Research and Consulting Division; and the Specialised Institutions Division. APRA's head office is in Sydney, with regional offices in Adelaide, Brisbane, Canberra, Melbourne and Perth. The Diversified Institutions Division, and Policy, Research and Consulting Division, along with APRA's administration, are based in the Sydney head office. The Specialised Institutions Division has staff in the Sydney head office as well as the regional offices.<sup>6</sup>

## Scope and conduct of the inquiry

1.8 In the Committee's *Reviews of the 1995-96 Annual Reports of the Reserve Bank of Australia, Australian Securities Commission, and the Insurance and Superannuation Commission*, the Committee recommended that APRA appear before the House Economics Committee once a year to report on the prudential supervision of the financial services industry.<sup>7</sup> The

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4 Department of the Treasury. 'Reform Of The Australian Financial System.' *Economic Round-Up*, Winter 1998. Canberra, AGPS, p 20.

5 Department of the Treasury. 'Reform Of The Australian Financial System.' *Economic Round-Up*, Winter 1998. Canberra, AGPS, p 20.

6 Australian Prudential Regulation Authority. *Annual Report 2000*. 2000. Sydney, APRA, pp 13-14.

7 House of Representatives Standing Committee on Economics, Finance and Public Administration. *Reviews of the 1995-96 Annual Reports of the Reserve Bank of Australia, Australian*

Committee indicated it wanted to review APRA's performance once the RBA no longer had prudential regulation responsibilities.<sup>8</sup>

- 1.9 On 29 March 1999, the Minister for Financial Services and Regulation provided the committee with a standing reference to review and report on APRA's supervision and prudential regulation of those areas of the financial services sector for which it has responsibility (see p *vii* for Terms of Reference).
- 1.10 On 4 September 2000, the Committee held its first public hearing with APRA in Canberra. Details of the hearing are set out in Appendix B. A copy of the transcript of evidence from the hearing has been published by the Committee and is available on the inquiry internet site<sup>9</sup> and from the committee secretariat.
- 1.11 Following the hearing, APRA made a submission to the Committee to follow up additional issues. A copy of that submission is at Appenix C and is also available on the inquiry internet site and from the committee secretariat.
- 1.12 APRA's *Annual Report 2000*, which was tabled in parliament on 5 September 2000, was also considered during the drafting of this report. While the *Annual Report 2000* fulfils all the necessary technical reporting requirements, the Committee believes that the annual report could be used more effectively by APRA as a regulatory and public accountability tool. APRA has a long way to go in its reporting activities before it reaches the high standards set by the RBA's *Annual Report 2000*. The Committee suggests a significant improvement by APRA in this area.
- 1.13 As the 4 September 2000 hearing was the first appearance by APRA before the Committee, the Committee addressed a wide range of issues relating to prudential regulation and APRA's administration. This report reflects the broad focus of that hearing. The report is structured into two chapters. Chapter 2 focuses on APRA's administration, including progress in the implementation of the Wallis Committee recommendations relating to

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*Securities Commission, and the Insurance and Superannuation Commission*. 1997. Canberra, AGPS, p 17.

<sup>8</sup> House of Representatives Standing Committee on Economics, Finance and Public Administration. *Review of The Reserve Bank of Australia Annual Report 1997-98: Interim Report*. 1999. Canberra, AGPS, p 10. See also House of Representatives Standing Committee on Economics, Finance and Public Administration. *Review of The Reserve Bank of Australia Annual Report 1997-9*. 1999. Canberra, AGPS, pp 22-31, and House of Representatives Standing Committee on Economics, Finance and Public Administration. *Review of The Reserve Bank of Australia Annual Report 1998-99: Interim Report*. 2000. Canberra, AGPS, p 43.

<sup>9</sup> <http://www.aph.gov.au/house/committee/efpa/apra9899/index.htm>.

prudential regulation, and the administration of levies. Chapter 3 addresses APRA's prudential regulatory activities across all regulated sectors.

- 1.14 As the Committee has a standing reference from the Minister for Financial Services to inquire into APRA's prudential regulation activities, this report is the first of a regular series. The Committee expects to review APRA's performance annually as it does biannually with the RBA.