

5 July 2013

Ms Fleur Grey
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Dear Ms Grey

**ASIC Consultation Paper 210 - Demutualisation approval procedure rules:
Minimum member participation requirement.**

Thank you for the opportunity to contribute to ASIC's review of its policy on considering requests from credit unions to cease the effect of the 25% minimum member participation requirement in the demutualisation approval procedure rules (DAPR).

The Customer Owned Banking Association (formerly known as Abacus – Australian Mutuals) represents Australia's customer owned banking sector, comprising 85 credit unions, nine mutual banks and seven mutual building societies. Our member banking institutions are Authorised Deposit-taking Institutions (ADIs) regulated by APRA.

The customer owned model is the proven alternative in retail banking, with 4.5 million customers, \$84bn in assets, 11% of household deposits and market-leading customer satisfaction.

Summary of our response to CP 210

We welcome ASIC's review of its approach to the DAPR and applications for relief from voting requirements, noting the time that has elapsed since the rule was formulated and the possibility of unintended consequences from unforeseen developments.

COBA and the customer owned banking sector as a whole remain strongly supportive of the principle of member participation imposed by the DAPR. ASIC should not provide relief to the DAPR where a restructuring proposal is a demutualisation, except where there are current prudential concerns.

Where the DAPR has been adopted into a mutual ADI's constitution, the minimum voting requirement should apply for all restructure proposals that would have the effect of the continuing entity ceasing to be, in substance, a mutual ADI. Except where prudential concerns are involved COBA would not see a case for ASIC providing relief from the DAPR in such cases.

We recognise that there may be cases where the DAPR is triggered on technical grounds and ASIC relief may be justified in limited circumstances where a restructuring proposal¹:

- Does not involve a demutualisation;
- Would see the entity, post restructure, continue to operate as a mutual ADI;
- Involve a clear benefit or improvement to members of the mutual ADI;
- Has no impact on member rights including access to reserves or voting entitlements; and
- Does not involve a fundamental change to the mutual ADI's identity, character, or business.

ASIC should be willing to consider relief in such cases but should consult stakeholders, such as COBA and COBA members, before making its decision. ASIC should take a conservative approach to exercising any relief on DAPR vote requirements and its assessment of whether any restructure is substantially changing the nature, future direction or structure of the entity.

A proposal to issue capital instruments does not necessarily trigger the DAPR because capital instruments that are "additional shares" are consistent with the Principles of Mutuality. "Investor shares" are expressly permitted under ASIC's Regulatory Guide 147 *Mutuality – Financial Institutions*. COBA is currently consulting with APRA and ASIC about Basel III regulatory capital instruments that comply with the mutuality tests in RG 147.

Background

As CP 210 notes the DAPR rule was developed by one of COBA's predecessor organisations, the industry association division of Cuscal, in consultation with ASIC. The impetus for the DAPR was work conducted by a 1999 credit union industry taskforce which highlighted a number of factors that remain relevant to the DAPR:

- Changes in the regulatory settings for mutual ADIs "post Wallis" that were perceived to have reduced safeguards on participation in demutualisation or conversion votes;
- The likelihood that unless a minimum participation threshold were set, restructure and demutualisation votes could be considered and passed by a very small quorum of credit union members (potentially consisting of staff and directors only);
- Use of vote participation thresholds for mutual banking organisations in other jurisdictions; and
- The importance of setting any threshold participation level at a low enough threshold to avoid the unintended impact of making governance decisions by interested members impossible.

Taking into account these and other factors the taskforce recommended the development of a permanent demutualisation procedure rule that it felt would balance these issues with a 25% participation requirement for special resolutions relating to trigger events².

Cuscal³ worked with ASIC to develop a demutualisation rule that would:

- Ensure that more than just a bare quorum of member votes would be required for votes that would determine the future of the credit union company;

¹ Possible examples could include adoption of mutual bank branding or other name changes, a merger with a mutual ADI that is not using 'credit union' as its category, establishment of a NOHC structure without compromising the mutual ADI operations or member rights.

² *Brand Strategy Project: Taskforce Reports "Demutualisation Risk Management: August 2000*

³ Cuscal as the Cuscal Industry Association, functions since transferred to COBA

- Place the authority for adopting and amending the rule in members' hands;
- Impose additional and supplementary procedures to the existing Schedule 4 Part 5 Corporations Act obligations for demutualisation proposals; and
- Include a relatively comprehensive list of triggers for the rule.

The rule was subsequently offered for consideration by credit unions with a disclosure pack to assist in member consideration, reviewed by ASIC. That material highlighted the prescriptive nature of the rule and the fact that, once adopted, any changes to the rule or removal (with the exception of extensions to member rights) would trigger the 25% participation requirement.

COBA and its members remain strongly of the view that the 25% participation hurdle is an appropriate participation threshold for restructure proposals that involve fundamental changes to the mutual ADI, including demutualisation.

CP 210 notes that ASIC's consideration of the minimum voting requirements in the DAPR and the circumstances, if any, in which it would consider applications for relief, has been prompted by a small number of requests for ASIC to cease the effect of DAPR in specific cases.

We note that these requests are for ASIC to intervene in the application of a company's constitution. Generally, these requests are concerned with the 25% minimum member participation requirements for the postal ballot and concerns that the 25% requirement is too high due to disengagement of members in the voting process.

It has been submitted that the 25% threshold is difficult to reach due to low levels of participation in resolutions on the general business of those entities. COBA's view is that 25% is demonstrably not impossible to reach⁴ and that participation in the general business of credit unions should not be compared to a decision to fundamentally change the nature of the mutual ADI.

CP 210 notes that removal of the 25% threshold may significantly increase the risk of enabling transactions that will impact the future direction of a credit union to be approved by a small number of members. This is precisely the risk that mutual ADIs have sought to mitigate through adoption of the DAPR and the reason that any changes to ASIC's approach or the rule are viewed with concern and caution by the mutual ADI sector.

COBA believes the critical issue is whether a restructuring proposal that triggers the DAPR will significantly change the identity, character, nature or business of the mutual ADI. If there is such a proposal, there is no case to switch off the DAPR. While the minimum voting requirements may add cost and expense to possible restructure votes, these are not sufficient grounds for ASIC to vary the rule or provide relief. The decision to adopt the DAPR was taken by individual mutual ADIs and their members as a conscious and clear means of strengthening member sovereignty and democratic principles.

If there is a proposal that triggers the DAPR but that will not significantly change the identity, character, nature or business of the mutual ADI, ASIC intervention in the interests of members (i.e. to avoid the unnecessary expenditure of members' funds) may be justified.

⁴In 2006, 50% of members of Statewest Credit Society voted in a demutualisation ballot. In 2008, 30-40% of Broadway Credit Union members voted in a voluntary liquidation and return of capital restructure. In 2012, 26% of members of Goldfields Credit Union voted in a demutualisation ballot.

Capacity for stakeholders such as COBA and COBA members to comment on particular proposals that are subject to requests to switch off the DAPR would assist ASIC to determine whether or not a proposal will significantly change the nature of a mutual ADI.

A commitment by ASIC for key stakeholder engagement would provide a greater degree of comfort to the mutual banking sector as a whole, which is seeking to ensure that regulators do not create incentives or smooth any path to demutualisations without proposals being the subject of active engagement with members, equitable and fair in their approach and allocations, and not for the enrichment of a minority.

Specific feedback

B1 We are considering whether we should change our current approach to circumstances in which we will publish and deliver a written notice to cease the effect of the 25% minimum member participation requirement.

B1Q1 Should ASIC consider giving a notice to switch off the 25% threshold? If not, why not? If yes, in what circumstances do you think we should do so?

COBA would support ASIC consideration of a notice to switch off the 25% vote participation threshold in limited, specific circumstances where the restructure proposed is not a demutualisation and will not significantly change the identity, character, nature and business of the mutual ADI.

The circumstances where ASIC should give consideration to relief include proposals where:

- The entity will continue, post the restructure, as a mutual ADI;
- There is a benefit to the entity's members (whether directly or through the mutual ADI overall) from the proposal;
- There are no impacts on member rights including entitlements to reserves and voting rights;
- No demutualisation is involved (or precursor to demutualisation);
- There is no fundamental change to the mutual ADI's identity, character or business (a view that would be informed by ASIC consultation with our industry);
- Where the rule is triggered only because of its drafting referring to "credit union" as opposed to "mutual ADI".

ASIC should not provide relief to the DAPR where a restructuring proposal is a demutualisation, except where there are current prudential concerns. Where the DAPR has been adopted into a mutual ADI's constitution, the minimum voting requirement should apply for all restructure proposals that would have the effect of the continuing entity ceasing to be, in substance, a mutual ADI. Except where prudential concerns are involved COBA would not see a case for ASIC providing relief from the DAPR in such cases.

B1Q2 What benefits do you consider will result from switching off the 25% threshold?

Where consideration is given to relief in the limited circumstances described above (B1Q1), the benefits that would result from switching off the 25% threshold include:

- Less expense for the mutual ADI if it chooses not to run an active member engagement plan (which would be required if the 25% threshold were to remain in place);
- Increased certainty for business planning and restructure proposals; and

- An easier path for mutual ADIs with the DAPR to introduce beneficial changes to their branding, structure or alliances within the mutual ADI sector.

B1Q3 What disadvantages do you consider will result from switching off the 25% threshold?

Switching off the 25% threshold would significantly increase the risk of enabling transactions that will impact the future direction of a mutual ADI to be approved by a small number of members. This could include hostile demutualisations or takeovers which are not in the best interests of members as a whole.

That is why the threshold should only be switched off for proposals that do not significantly impact the future direction of the mutual ADI.

B1Q4 What impact, if any, would switching off the 25% threshold have on your business costs? How would you manage potential changes?

N/A

B1Q5 Are there any practical problems with the implementation of this proposal? Please give details.

COBA acknowledges that a flexible and discretionary approach to ASIC's power to switch off all or parts of the DAPR creates uncertainty. However, this uncertainty is not new and the original rationale for ASIC's 'veto' power was to respond to unintended impacts and unforeseen issues.

The uncertainty can be ameliorated by ASIC making clear that the power will be used conservatively, taking into account the results of its consultation with the mutual banking industry as appropriate.

B2 We are considering whether we should impose conditions that require the credit union to instead comply with a lower threshold for member participation in the postal ballot.

B2Q1 Do you think that 25% is an appropriate threshold for the minimum member participation requirement in the postal ballot? Why or why not? If not, what do you think would be an appropriate level? Why?

COBA supports 25% (or a lower threshold if a particular mutual has a lower threshold in its constitution) as an appropriate threshold. It is low enough to be achievable but high enough to ensure meaningful member participation in a demutualisation or significant restructuring proposal.

B2Q2 What benefits do you consider will result from altering the 25% threshold for the minimum member participation requirement in the postal ballot?

N/A

B2Q3 What disadvantages do you consider will result from altering the 25% threshold for the minimum member participating requirement in the postal ballot?

COBA's view is that this would create uncertainty and unnecessary complexity. Either you have a minimum threshold or you don't have a minimum threshold.

B2Q4 What impact, if any, would altering the 25% threshold have on your business costs? How would you manage potential changes?

N/A

B2Q5 Are there any practical problems with the implementation of this proposal? Please give details.

N/A

B2Q6 If possible, please provide any available data relating to voting participation levels in support of your answers.

In 2006, 50% of members of Statewest Credit Society voted in a demutualisation ballot. In 2008, 30-40% of Broadway Credit Union members voted in a voluntary liquidation and return of capital restructure. In 2012, 26% of members of Goldfields Credit Union voted in a demutualization ballot.

In 2009, 19% of Mystate Credit Union members voted in a demutualisation ballot that did not require 25% participation. In 2011, 22% of Maleny Credit Union members voted in a merger proposal that did not require 25% participation.

Please contact me on 02 8035 8420 or Luke Lawler (Senior Manager, Public Affairs) on 02 8035 8448 to discuss any aspect of this submission.

Yours sincerely

A handwritten signature in blue ink, appearing to read 'Louise', with a long horizontal flourish extending to the right.

LOUISE PETSCHLER
Chief Executive Officer