



AUSTRALIAN CATHOLIC BISHOPS CONFERENCE

General Secretariat

15 February 2016

Mr Andrew Duffy
Investments Managers and Superannuation
Australian Securities and Investments Commission
GPO Box 9827
SYDNEY NSW 2001
Email: Andrew.Duffy@asic.gov.au

Dear Mr Duffy,

Submission in response to ASIC's policy proposal for regulation of Charitable Investment Fundraisers

Thank you for your letter dated 7 January 2016 and for the opportunity to comment on revised policy proposals for the regulation of Charitable Investment Fundraisers (CIFs).

Your letter was addressed to the Rev Brian Lucas, who is now the National Director of Catholic Mission. Fr Brian has been retained by the Bishops Conference as Special Counsel to assist with matters such as this. The Australian Catholic Bishops Conference (ACBC) appointed me as the General Secretary in January.

The ACBC is a permanent institution of the Catholic Church in Australia (the Church) and the instrumentality used by the Australian Catholic Bishops to act nationally and address issues of national significance.

APRA and ASIC regulation

You may be aware that the Treasurer, the Hon Scott Morrison MP, wrote to the ACBC on 10 November 2015 to advise of the Australian Prudential Regulation Authority's (APRA's) decision on Religious Charitable Development Funds (RCDFs), including Catholic Development Funds (CDFs), in the light of the report of the Financial Systems Inquiry (FSI). APRA wrote to each of the CDFs outlining their position and processes to be undertaken. The correspondence is **attached**.

The decision means further restrictions on the operation of RCDFs. The ACBC has since been in contact with the APRA to discuss the implementation of this decision. I understand RCDFs will be invited to meet with APRA later this year and we will be invited to comment on transitional arrangements. It would seem appropriate for the Australian Securities and Investments Commission (ASIC) to coordinate with APRA to avoid regulatory confusion.

The regulatory environment should be complementary and consistent. For example, ASIC's new C5 proposal to prohibit any short term withdrawals if "retail" investors are present, ignores the security and liquidity provisions in place within the combined CDFs. There is no justification for imposing this restriction in our view.

ASIC should mirror the final APRA negotiated position. Therefore, we would argue it is premature to be concluding CP207 proposals at this stage.

Potential Impact on the Australian Community

The ACBC is pleased ASIC has revised its original proposal but still has some concern that it is continuing with modifications to current conditions of relief and proposing new ones which significantly increase their impact on CDFs. If adopted, they would result in significant loss of income for many CDFs, impacting on those providing social, educational, health and welfare services to Indigenous Australians, migrants, refugees, young people, women in crisis, the frail aged and the homeless and people with disability.

The work of CDFs in providing services to associated entities is in a different category with respect to regulatory policy and so our observations below relate only to "retail" or "parishioner" participants in the CDF.

Catholic Development Funds enable good works

CDFs have played a central role in the delivery of the Church's mission for almost 60 years, enabling the provision of schools, churches and other vital community infrastructure.

CDFs are not-for-profit and charitable organisations with a clear mission. They take a prudent and ethical approach to carefully managing Church and laity deposits for the benefit of the Church and broad community. They are not the types of risk-oriented organisations chasing windfall profits that led to the international turmoil of the Global Financial Crisis.

Today 24 CDFs are operating in dioceses throughout Australia. Each CDF is working for the mission of their respective diocese, and the mission of the whole Catholic Church, in helping to build today's Church community by providing funds for schools, churches,

retirement villages, aged care facilities and hospitals. Integral to achieving this is the investment support received from Church organisations and Catholic individuals.

CDFs provide operational and business services for parishes, schools and associated church organisations, as well as investment accounts for individuals. Each CDF has a relationship with a bank, which allows for the provision of the products and services required. The CDFs assist in the accomplishment of the Church's mission by financing capital projects and providing income for dioceses through prudent financial management.

The Catholic Church is a major provider of religious services, schools, health, retirement, aged care and social services. The Catholic Church consists of more than 1,300 parishes in local communities across the nation. It teaches more than 750,000 children, employs almost 60,000 teachers in more than 1,700 schools in every state and territory of Australia. It operates 75 hospitals with 9,500 beds. It provides almost 20,000 residential aged care beds and eight dedicated hospices. Catholic social services comprise 59 agencies employing around 12,000 people, with 4,000 voluntary contributors to this work. The social services network provides community services to more than one million Australians every year, with programs valued at around \$600 million.

The pooling of funds from Catholic individuals, schools, parishes and other organisations has allowed many Catholic entities access to loan funding to expand their charitable works, expansion that would not have been possible because they may not have been able to borrow from other lenders and/or afford their lending rates, fees and charges.

CDF Facts

Liquidity

Of the total combined CDFs assets of \$7.49B, \$3.9B is invested (i.e. not on-lent). Of the \$3.9B, 82.5% is invested in cash/bank term deposits/negotiable certificates of deposit, 10.5% in bank floating rate notes, bills and bonds, 4.75% invested with other CDFs and only 2.25% in other investments. \$2.5B of the \$3.9B (65%) is invested for a term of less than 90 days.

91.5% of deposits are from associated entities and 8.5% from laity.

There is more than ample liquidity available within the CDF environment to cover individual fund liquidity needs.

Lending

CDFs only lend within the Church to associated entities and do not lend into speculative scenarios. The underlying customer profile is one of long-term stability and in many cases, government funded services.

Accumulated reserves

Collectively CDFs have total reserves of \$522 million on total customer investments of \$6.97B.¹

Laity (non-associated entity) investments amount to only \$585M or 8.5% of total combined customer investments. They are more than covered from a security/liquidity perspective.

CDFs have a different business model

ASIC's use of wholesale and retail investor terms does not represent the character or the relationship which clients of a CDF have with their CDF. CDFs have controlled and associated entities plus laity. This is not the same as an uninformed public.

The CDF business model demonstrates long-term stability and strong participant loyalty. During the Global Financial Crisis liquidity management was well maintained and there were no requests for withdrawal of funds which were not met on time in accordance with the participant's request.

In addition to the careful and prudent management of liquidity and the level of reserves the clients of CDFs also have the added protection of an indemnity from the bishop of each diocese funded from CDF reserves plus the net assets of the diocese if need be. CDFs are not the same as a standalone managed investment scheme.

Specific ASIC proposals

We are concerned by ASIC's insistence that CDF customers be warned of the potential for loss of their investment (C6 and now also C8). This is posited by ASIC in the absence of any known CDF customer investment loss to date. It also ignores the security behind the investment in the form of significant reserves and the net assets of each diocese.

We fail to see the need for an Australian financial services licence (AFSL) regime for CDFs. As ASIC itself acknowledges in CP207 at #4, investors are not attracted to CDFs for reasons of making a financial gain. One wonders then, why licensed financial advice is required when a customer has already made this decision. As mentioned in the ACBC's July 2013 submission, CDFs do not offer financial advice on products offered. The compliance costs to meet AFSL and licensed representative requirements would be prohibitive on a relatively small component of overall CDFs' investments and coupled with the expected loss of money due to the 31-day rule, probably unviable.

We would continue to argue for the inclusion of clergy and employees of associated entities, in the definition of associated entities because of their relationship to the Church, their commitment to its mission and their informed knowledge of the operation

¹ Australian CDF's Aggregated Annual Financial Statements 2014/2015

of their CDF. Additionally, CDFs provide a cost-effective and convenient facility for payroll management for employees.

Original ASIC concerns in CP207 surrounding shadow banking, competitive neutrality, investor risk and investor investment motivations are not borne out in the business models used by CDFs.

Comments and further clarification required

Proposal 1: Licensing

Original proposal C2

Do we take it that this proposal remains as is with the new commentary under Current Proposal being additional? If so, the text “CIFs that accept new investment fundraising from retail investors” appears to exclude existing investments already held for that category of investor. Is this the case?

Current proposal

The definition of a charity at RG 87.10 is “ ... religious ,educational, community and other organisations that are recognised in law as being formed for religious, educational, community and other charitable purposes.”

The current proposal states “... will treat as associated entities, entities that are connected with the charitable investment fundraiser by being subject to common control or having a common charitable objective”.

The definition of “associated entity” is unclear. Associated entities will include mix of incorporated and unincorporated entities. For the reasons set out above, clergy and employees should be treated as associated entities.

The New South Wales *Charitable Fundraising Act 1991* could provide a model for defining an associated entity.

Proposal 2: Prohibition on issue of at-call or short-term products

Current proposal

We found points (a), (b), (c) and (d) under this proposal most difficult to decipher and interpret given the use of terms that do not apply to CDFs.

We would ask for further clarification on what these points mean for non-associated entities.

Another point that needs some clarification is that there is no definition as to how it would be determined or who would decide when the following events have occurred - “materially increase the risk of a CIF being unable to meet retail investors’ repayment rights” and “if there is a liquidity event”.

There is a second point (d) that refers to “...restricting CIFs from offering cheques, EFTPOS, ATM and BPAY facilities to retail investors”. It is not clear why this has been included when the existing Banking Exemption issued by APRA does not permit the provision of these services to non-associated investors.

It would help if the approach undertaken by ASIC aligns with that adopted by APRA. The two agencies should ensure their approach is the same; otherwise, there will be unnecessary confusion and a higher risk of non-compliance.

Prohibiting a CIF from 1 January 2018 from providing an associated entity with an at-call or short-term product if a CIF also has any non-associated investors is harsh and unreasonable.

Regarding the new C5 proposal, we would argue that lay non associated entities should be treated in the same manner as controlled and associated entities in the event of a liquidity issue.

Proposal 3: Investor acknowledgement requirement

Any requirement to have a non-associated entity sign an acknowledgment is in our view flawed or of dubious value. We take it from the commentary that ASIC has doubts as well. ASIC should scrap this option.

Proposal 4: Restricted terms

This proposal is inconsistent with the position taken by APRA, which has indicated that it intends to only apply the restriction to non-associated investors.

Proposal 5: Additional disclosure requirements

We view that this proposal is only in relation to CIFs that have non associated money. We strongly oppose additional investor disclosures that are provocative and focus on potential loss of some or all of their investment not the extent of regulatory protection. This unnecessarily raises investor fears and damages the good reputation of CDF’s.

Proposal 6: Financial reporting

All CDFs prepare audited financial statements.

Proposal 7: Identification statement

We view that this proposal is only in relation to CIFs that have non associated money.

Proposal 8: Breach reporting

This requirement would be an overreach. At most, breach reporting should only apply to CDFs with respect to their non-associated entities.

Proposal 9: Commencement date

There is again reference to “new funds from retail clients”. The proposal as it reads does not differentiate between associated and non-associated at call/short term investments. The proposal is unclear on the treatment of existing funds held for non-associated investors.

There should be a consultation process in line with that proposed by APRA.

In the event that a CDF which currently has non associated investors and wishes to move solely to associated entities, there should be a grandfathering of the existing non associated investors and that they be allowed to run down over a longer period without any of the proposed requirements.

Additional ASIC questions

In response to the four specific questions raised by ASIC, we advise as follows:

- (a) The impact of the proposal will result in additional compliance costs. These “costs” will actually be in the form of loss of interest income on funds from non-associated entities that will have to be relinquished to maintain a compliant status. Further costs may emanate from the CDF having to potentially raise a Line of Credit from another CDF or a bank to meet demand for loan funding, as this source of funds is more expensive than the existing investments from non-associated entities.
- (b) Not applicable.
- (c) A significant negative impact will be the inconvenience, disruption and confusion that will be incurred by clergy and employees in having to discontinue holding their investments with their local CDF and having to establish a direct banking relationship with an Authorised Deposit-Taking Institution (ADI). No positive impact or benefit would emanate from this proposal.
- (d) CDFs are reluctant to apply for an AFS licence given the complexities and potential costs involved. Many if not all CDFs will therefore be forced to discontinue offering investment interests to non-associated investors if the proposals are implemented.

Conclusion

CDFs have been operating successfully for almost 60 years, aided by strong governance and compliance structures. CDFs are a successful model of cooperation for pooling resources for the common good. They are not like banks or other registered finance companies.

The proposal as it stands, resulting in the loss of non-associated entities' money used by CDFs to further the charitable work of the Church, will inhibit the capital development in the Church's social, educational, welfare and health services to the community.

The ACBC would like to see the current exemptions continue in their current form given the long and successful history of CDFs.

We would appreciate a meeting to discuss this with you as soon as convenient.

Yours sincerely,

A handwritten signature in black ink, reading "Stephen Hackett msc". The signature is written in a cursive style with a large, sweeping flourish that extends from the end of the name.

Rev Dr Stephen P Hackett msc
General Secretary