2016-2017

THE PARLIAMENT OF THE COMMONWEALTH OF AUSTRALIA

HOUSE OF REPRESENTATIVES

MAJOR BANK LEVY BILL 2017

TREASURY LAWS AMENDMENT (MAJOR BANK LEVY) BILL 2017

EXPLANATORY MEMORANDUM

(Circulated by authority of the
Treasurer, the Hon Scott Morrison MP)

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Glossary

The following abbreviations and acronyms are used throughout this explanatory memorandum.

Abbreviation	***Definition***
ADI	authorised deposit-taking institution
APRA	Australian Prudential Regulation Authority
APRA Act	*Australian Prudential Regulation Authority Act 1998*
Collection of Data Act	*Financial Sector (Collection of Data) Act 2001*
Commissioner	Commissioner of Taxation
GDP	Gross Domestic Product
ITAA 1997	*Income Tax Assessment Act 1997*
PAYG	Pay-As-You-Go
Major Bank Levy Act	*Major Bank Levy Act 2017*
Major Bank Levy Bill	Major Bank Levy Bill 2017
MBL benefits	major bank levy benefits
RBA	Reserve Bank of Australia
TAA 1953	*Taxation Administration Act 1953*
Treasury Laws Amendment Bill	Treasury Laws Amendment (Major Bank Levy) Bill 2017

General outline and financial impact

Major bank levy

The Major Bank Levy Bill 2017 (Major Bank Levy Bill) will introduce a levy on authorised deposit-taking institutions (ADIs) with total liabilities of greater than $100 billion. The levy is imposed at a rate of 0.015 per cent on certain liabilities of the ADI that are reported to the Australian Prudential Regulation Authority (APRA) on a quarterly basis under a reporting standard.

Schedule 1 to the Treasury Laws Amendment (Major Bank Levy) Bill 2017 (the Treasury Laws Amendment Bill) amends the *Australian Prudential Regulation Authority Act 1998* (APRA Act), the *Financial Sector (Collection of Data) Act 2001* (Collection of Data Act), the *Income Tax Assessment Act 1997* (ITAA 1997) and the *Taxation Administration Act 1953* (TAA 1953) to specify certain administrative features relating to the major bank levy, including the requirement that the levy is payable to the Commissioner of Taxation (Commissioner) quarterly.

Date of effect: 1 July 2017

Proposal announced: The measure was announced on 9 May 2017 as part of the 2017-18 Budget.

Financial impact: The measure has these revenue implications:

2016-17	***2017-18***	***2018-19***	***2019-20***	***2020-21***
—	$1,600.0m	$1,500.0m	$1,500.0m	$1,600.0m

These figures are the implications for the fiscal balance, totalling $6.2 billion over those years. The implications for the underlying cash balance are $5.5 billion over the same period.

Human rights implications: These Bills do not raise any human rights issue. See *Statement of Compatibility with Human Rights* — paragraphs 1.83 to 1.87.

Compliance cost impact: Low.

Summary of regulation impact statement

Regulation impact on business

Impact: Total compliance costs of $15 million, or $1.5 million per annum, across the affected banks over a ten year period.

Main points:

- APRA will create a new reporting form to collect the data required to calculate the major bank levy.
- While this will impose some additional compliance costs, banks already collect much of the data required for existing APRA reporting forms and other purposes.
- Any risks to financial market disruption arising from the major bank levy have been minimised by its design.
- The major bank levy should have a negligible impact on the real economy.

Chapter 1
Major bank levy

Outline of chapter

1.1 The Major Bank Levy Bill will introduce a levy on ADIs with total liabilities of greater than $100 billion. The levy is imposed at a rate of 0.015 per cent on certain liabilities of the ADI that are reported to APRA on a quarterly basis under a reporting standard.

1.2 Schedule 1 to the Treasury Laws Amendment Bill amends the APRA Act, the Collection of Data Act, the ITAA 1997 and the TAA 1953 to specify certain administrative features relating to the major bank levy, including the requirement that the levy is payable to the Commissioner quarterly.

Context of amendments

1.3 In the 2017-18 Budget the Government announced that it would introduce a levy on major banks with liabilities greater than $100 billion (indexed to grow in line with nominal Gross Domestic Product (GDP)).

1.4 The major bank levy will raise $6.2 billion over four years, net of interactions with other taxes. This represents a fair additional contribution from Australia's highly profitable major banks.

1.5 It will contribute to budget repair over the forward estimates period. The levy will also contribute to strengthening the structural position of the budget for the long term — providing greater fiscal capacity to accommodate shocks such as those seen in the global financial crisis.

1.6 The major bank levy is similar to bank levies imposed in other advanced countries, recognising that large leveraged banks are a source of systemic risk in the financial system and the wider economy. Those risks were made evident in the global financial crisis.

1.7 It will complement prudential reforms being implemented by the Government and APRA to improve financial system resilience. These reforms include:

- setting bank capital levels such that they are 'unquestionably strong';
- strengthening APRA's crisis management powers; and
- ensuring banks have appropriate loss absorbing capacity.

1.8 APRA has confirmed that the payment of the major bank levy will not have a material impact on the resilience of the banking system and that it does not harm its prudential policy objectives.

1.9 The major bank levy will also contribute to a more level playing field for smaller, often regional, banks and non-bank competitors. As the House of Representatives Standing Committee on Economics report on the four largest banks found, the major banks' size and market dominance affords them significant funding cost advantages and pricing power at the expense of their customers.

Summary of new law

1.10 The Major Bank Levy Bill will introduce a levy on ADIs with total liabilities of greater than $100 billion. The $100 billion threshold will be indexed to grow in line with nominal GDP.

1.11 The levy is imposed at a rate of 0.015 per cent on certain liabilities of the ADI that are reported to APRA each quarter. The amount of liabilities on which the major bank levy will be payable is the total reported liabilities of the ADI for the quarter, reduced by the sum of:

- the ADI's total Additional Tier 1 Capital at the end of the quarter;
- the ADI's total holdings of deposits protected by the Financial Claims Scheme at the end of the quarter;
- an amount equal to the lesser of the derivative assets and derivative liabilities at the end of the quarter in relation to the ADI; and
- the exchange settlement account balance held with the Reserve Bank of Australia (RBA) for the quarter in relation to the ADI.

1.12 Schedule 1 to the Treasury Laws Amendment Bill amends various Acts to specify certain administrative features relating to the major bank levy. In particular, the amendments:

- modify the TAA 1953 to:
  - specify that the major bank levy is payable to the Commissioner;
  - ensure that the ordinary collection and recovery provisions apply in relation to the levy;
  - introduce an anti-avoidance law for the levy; and
  - allow the Commissioner to give information relating to the levy to APRA;
- modify the ITAA 1997 so that the $100 billion threshold is indexed to grow in line with nominal GDP;
- modify the Collection of Data Act to allow the APRA reporting standards to include information relating to amounts for the purposes of the major bank levy; and
- modify the APRA Act to allow APRA to provide information relating to the major bank levy to the Commissioner.

Comparison of key features of new law and current law

New law	*Current law*
The major bank levy will apply to ADIs with total liabilities of greater than $100 billion. The $100 billion threshold will be indexed to grow in line with nominal GDP. The levy is imposed at a rate of 0.015 per cent on certain liabilities of the ADI that are reported to APRA each quarter. The amount of liabilities on which the major bank levy will be payable is the total reported liabilities of the ADI for the quarter, reduced by the sum of: • the ADI's total Additional Tier 1 Capital at the end of the quarter; • the ADI's total holdings of deposits protected by the Financial Claims Scheme at the end of the quarter;	No equivalent.

• an amount equal to the lesser of the derivative assets and derivative liabilities at the end of the quarter in relation to the ADI; and • the exchange settlement account balance held with the RBA for the quarter in relation to the ADI. The major bank levy is payable to the Commissioner quarterly.	

Detailed explanation of new law

1.13 The Major Bank Levy Bill 2017 will introduce the *Major Bank Levy Act 2017* (Major Bank Levy Act). ***[Major Bank Levy Bill, section 1 of the Major Bank Levy Act]***

Who is liable to pay the major bank levy

1.14 The major bank levy will be imposed on an ADI for a quarter starting on or after 1 July 2017 if the ADI's total liabilities amount for the quarter exceeds the levy threshold for the quarter. ***[Major Bank Levy Bill, subsubsection 4(1) of the Major Bank Levy Act]***

1.15 An ***ADI*** is a body corporate that is an ADI for the purposes of the *Banking Act 1959*. An ADI is defined under that Act to be a body corporate in relation to which an authority under subsection 9(3) of that Act is in force. ***[Major Bank Levy Bill, definition of 'ADI' in section 3 of the Major Bank Levy Act]***

1.16 In this regard, the major bank levy applies to a body corporate that is a licensed ADI. This includes the business of the ADI ordinarily described as 'foreign bank branch' activity, but does not include other body corporates in the ADI's group (such as foreign or non-banking subsidiaries, or non-operating holding companies).

1.17 A ***quarter*** is each period of 3 months ending 31 March, 30 June, 30 September or 31 December. ***[Major Bank Levy Bill, definition of 'quarter' in section 3 of the Major Bank Levy Act]***

1.18 The ***total liabilities amount*** in relation to an ADI for a quarter is the amount equal to the total liabilities of the ADI for the quarter, as reported under an applicable reporting standard. ***[Major Bank Levy Bill, definition of 'total liabilities amount' in section 3 and subsection 4(2) of the Major Bank Levy Act]***

1.19 An ***applicable reporting standard*** is a standard that:

- is determined by APRA under section 13 of the Collection of Data Act; and
- relates to reporting amounts for the purposes of this Act (whether or not it also relates to other matters).

[Major Bank Levy Bill, definition of 'applicable reporting standard' in section 3 of the Major Bank Levy Act]

1.20 In this regard, the total liabilities amount for a quarter, and other amounts for a quarter that are relevant to working out the major bank levy, must be worked out in accordance with:

- accounting principles — that is, in accordance with accounting standards or, if there are no relevant accounting standards, in accordance with authoritative pronouncements of the Australian Accounting Standards Board that apply to the preparation of financial standards (see the definition of *accounting principles* in subsection 995-1(1) of the ITAA 1997); and
- any applicable legislative instrument made by the Minister — a legislative instrument made for these purposes may make provisions in relation to a matter by applying, adopting or incorporating any matter contained in any other instrument or writing as in force from time to time and has effect despite anything in subsection 14(2) of the *Legislative Instruments Act 2003*.

[Major Bank Levy Bill, sections 7 and 8 of the Major Bank Levy Act]

1.21 The ***levy threshold***, for the quarter starting 1 July 2017, is $100 billion. ***[Major Bank Levy Bill, definition of 'levy threshold' in section 3 and subsection 4(3) of the Major Bank Levy Act]***

1.22 The levy threshold is indexed quarterly by:

- multiplying the amount ($100 billion) by the indexation factor for the particular quarter; and
- rounding the result down to the nearest $1 million.

[Major Bank Levy Bill, subsection 4(3) of the Major Bank Levy Act; Treasury Laws Amendment Bill, Schedule 1, items 5 and 9, item 14 of the table in subsection 960-265 and subsection 960-290(1) of the ITAA 1997]

1.23 The levy threshold is not indexed if the indexation factor is one or less. ***[Treasury Laws Amendment Bill, Schedule 1, item 9, subsection 960-290(2) of the ITAA 1997]***

1.24 The indexation factor for a particular quarter is worked out using the formula:

$$\frac{\text{GDP number for the preceding quarter}}{\text{GDP number for base quarter}}$$

[Treasury Laws Amendment Bill, Schedule 1, items 9 and 11, subsection 960-290(3) and the definition of 'indexation factor' in subsection 995-1(1) of the ITAA 1997]

1.25 The indexation factor is worked out to three decimal places, rounding up if the fourth decimal place is five or more. ***[Treasury Laws Amendment Bill, Schedule 1, item 9, subsection 960-290(4) of the ITAA 1997]***

1.26 For the purposes of working out the indexation factor:

- the GDP number for the base quarter is the estimate that is, at the end of the quarter to which indexation is to be applied, the estimate of the GDP: Current Prices — Seasonally Adjusted most recently published by the Australian Statistician for the quarter ending on 30 June 2017; and
- the GDP number for the preceding quarter is the estimate of the GDP: Current Prices — Seasonally Adjusted first published by the Australian Statistician for the quarter preceding the quarter to which the indexation is to be applied.

[Treasury Laws Amendment Bill, Schedule 1, item 9, subsection 960-290(3) of the ITAA 1997]

1.27 In this regard, indexation will first apply to the quarter starting on 1 October 2017 (which ends on 31 December 2017). The nominal GDP for that quarter is due to be published on 7 March 2018, which is after the date on which the liability for major bank arises. Therefore, the indexation factor is worked out by reference to the nominal GDP published by the Australian Statistician for the quarter preceding the quarter to which the indexation is to be applied.

1.28 In addition, if the nominal GDP for a particular quarter is revised in a subsequent quarter, the denominator in the indexation formula is based on the estimate of the GDP: Current Prices — Seasonally Adjusted that is most recently published by the Australian Statistician for the quarter ending on 30 June 2017.

1.29 Consequential amendments switch off general provisions in the ITAA 1997 that apply to indexation factors. ***[Treasury Laws Amendment Bill, Schedule 1, items 6 to 8 and 12, subsections 960-270(3), 960-275(6), 960-280(6) and the definition of 'index number' in subsection 995-1(1) of the ITAA 1997]***

Example 1.1

The major bank levy first applies for the quarter starting on 1 July 2017 (which ends on 30 September 2107). The levy threshold for that quarter is $100 billion.

The levy threshold ($100 billion) will be indexed for the quarter starting on 1 October 2017 (which ends on 31 December 2017). The indexation factor for that quarter will be worked out using the following formula:

$$\frac{\text{GDP number for the quarter ending on 30 September 2017 (as published in December 2017)}}{\text{GDP number for the quarter ending 30 June 2017 (as published in December 2017).}}$$

The levy threshold ($100 billion) will be indexed again for the quarter starting on 1 January 2018 (which ends on 31 March 2018). The indexation factor for that quarter will be worked out using the following formula:

$$\frac{\text{GDP number for the quarter ending on 31 December 2017 (as published in March 2018)}}{\text{GDP number for the quarter ending 30 June 2017 (as published in March 2018).}}$$

Working out the amount of the major bank levy

1.30 The amount of the levy payable by the ADI for a quarter is 0.015 per cent of the applicable liabilities amount for the quarter in relation to the ADI. ***[Major Bank Levy Bill, subsection 5(1) of the Major Bank Levy Act]***

1.31 The ***applicable liabilities amount*** for the quarter is the total liabilities amount of the ADI for the quarter, reduced by the sum of:

- the total Additional Tier 1 Capital for the quarter in relation to the ADI, as reported under an applicable reporting standard;
  - Additional Tier 1 Capital are the liabilities that the ADI owes in relation to Additional Tier 1 Capital instruments that fall within the meaning of the prudential standards

determined by APRA and in force under section 11AF of the *Banking Act 1959*;

- the total holdings of deposits held, to the extent that they would be protected by the ADI Financial Claims Scheme, for the quarter in relation to the ADI, as reported under an applicable reporting standard;

- an amount equal to the lesser of the derivative assets and derivative liabilities at the end of the quarter in relation to the ADI, as reported under an applicable reporting standard;

  – a derivative is, broadly, an agreement or instrument the value of which changes in response to a specific underlying variable or variables, requires no or limited initial net investment and is settled at a future date;

- the exchange settlement account balance, held with the RBA, for the quarter in relation to the ADI, as reported under an applicable reporting standard;

  – an exchange settlement account is an account held at the RBA which is used for the daily final settlement obligations between exchange settlement account holders; and

- any other amounts of a kind determined by the Minister in a legislative instrument — a legislative instrument made for these purposes may make provisions in relation to a matter by applying, adopting or incorporating any matter contained in any other instrument or writing as in force from time to time and has effect despite anything in subsection 14(2) of the *Legislative Instruments Act 2003*.

[Major Bank Levy Bill, definitions of 'applicable liabilities amount' and 'ADI financial claims scheme' in section 3 and subsections 5(2) and (4) to (6) of the Major Bank Levy Act]

1.32 The methods for working out any of these amounts may be set out in an applicable reporting standard (including the standard mentioned in subsection 4(2)). ***[Major Bank Levy Bill, subsection 5(3) of the Major Bank Levy Act]***

1.33 This means that the amount determining the levy for each ADI should be in line with the amounts that the ADI reports to APRA under a standard determined under section 13 of the Collection of Data Act.

1.34 Section 3 of the Collection of Data Act sets out that the object of that Act is to enable APRA to collect information for a range of purposes. An amendment is being made to that Act to clarify that those purposes include the purpose of reporting amounts for the purposes of the major bank levy. ***[Treasury Laws Amendment Bill, Schedule 1, item 2, paragraph (3)(1)(d) of the Collection of Data Act]***

1.35 The Collection of Data Act is also being amended to clarify that the APRA reporting standards can include matters that relate to the reporting of amounts for the purposes of the Major Bank Levy Act. ***[Treasury Laws Amendment Bill, Schedule 1, item 3, subsection 13(2B) of the Collection of Data Act]***

1.36 A reporting standard made for these purposes may make provision in relation to a matter that relates to these amounts by applying, adopting or incorporating any matter contained in any other instrument or writing as in force from time to time and has effect despite anything in subsection 14(2) of the *Legislative Instruments Act 2003*. ***[Treasury Laws Amendment Bill, Schedule 1, item 3, subsections 13(2C) and (2D) of the Collection of Data Act]***

1.37 Consequently, the instructions for filling in a report prescribed under the standard may refer to definitions and instructions outlined elsewhere, including those in this Act and any legislative instruments made under this Act.

1.38 Consistent with amounts currently being reported under a standard determined under section 13 of the Collection of Data Act, entities are required to comply with reporting requirements, including having appropriate quality control processes in place.

1.39 The amounts for a quarter are generally the relevant amount as at the end of the last day in the quarter. ***[Major Bank Levy Bill, subsection 6(1) of the Major Bank Levy Act]***

1.40 However, for the following amounts, the relevant amounts for a quarter are worked out using the method statement in subsection 6(3):

- the total liabilities amount, but only to the extent that they consist of liabilities relating to:
  - debt securities — debt securities are borrowed funds that must be repaid and that can be traded, including instruments like commercial paper and bonds;
  - repurchase agreements;
  - loans between the ADI concerned and another ADI;

  - loans between the ADI concerned and a foreign bank — a foreign bank is defined in section 128A of the *Income Tax Assessment Act 1936* to mean a non-resident (foreign) company that carries on banking business;

- the exchange settlement account balance held with the RBA; and

- any amount of a kind determined by the Minister in a legislative instrument — a legislative instrument made for these purposes may make provisions in relation to a matter by applying, adopting or incorporating any matter contained in any other instrument or writing as in force from time to time and has effect despite anything in subsection 14(2) of the *Legislative Instruments Act 2003*.

[Major Bank Levy Bill, subsections 6(2) and (4) to (6) of the Major Bank Levy Act]

1.41 In these cases, the relevant amount for a quarter is worked out on a quarterly average basis applying the following steps:

- Step 1 — For each day in the quarter, work out the relevant amount as at the end of that day.

- Step 2 — Add all the step 1 amounts together.

- Step 3 — Divide the step 2 amount by the total number of days in the quarter.

[Major Bank Levy Bill, subsection 6(3) of the Major Bank Levy Act]

1.42 The requirement for these amounts to be quarterly averaged will minimise any market disruptions resulting from the incentives to reduce outstanding liabilities immediately before the end of a quarter.

Major bank levy is payable to the Commissioner of Taxation

1.43 The Commissioner has the general administration of the major bank levy. As a consequence, the Major Bank Levy Act will be a *taxation law* (as defined in subsection 995-1(1) of the ITAA 1997). ***[Treasury Laws Amendment Bill, Schedule 1, items 20 and 21, sections 356-1 and 356-10 of Schedule 1 to the TAA 1953]***

1.44 An ADI that is liable to pay the major bank levy must give the Commissioner a quarterly return relating to the levy. An amount of levy is payable when an ADI's last Pay-As-You-Go (PAYG) instalment within an instalment quarter is due. ***[Treasury Laws Amendment Bill, Schedule 1, item 15, section 115-1 of Schedule 1 to the TAA 1953]***

1.45 If an ADI incurs expenditure for major bank levy, the ADI can claim an income tax deduction for the whole of the amount incurred. ***[Treasury Laws Amendment Bill, Schedule 1, item 4, paragraph 25-5(1)(cb) of the ITAA 1997]***

1.46 The return relating to the levy must be given by the ADI to the Commissioner in the approved form on or before the MBL reporting day for the quarter. ***[Treasury Laws Amendment Bill, Schedule 1, item 15, subsections 115-5(1) and (2) of Schedule 1 to the TAA 1953]***

1.47 The ***MBL reporting day*** for the quarter is the day by which the ADI is required to give APRA a report in accordance with an APRA reporting standard that:

- relates to the quarter; and
- states the total liabilities amount for the purposes of the major bank levy for the quarter in relation to the ADI.

[Treasury Laws Amendment Bill, Schedule 1, items 13 and 15, definition of 'MBL reporting day' in subsection 995-1(1) of the ITAA 1997 and subsection 115-5(3) of Schedule 1 to the TAA 1953]

1.48 The Commissioner is taken to have made an assessment of the amount of major bank levy when an ADI gives a return to the Commissioner. ***[Treasury Laws Amendment Bill, Schedule 1, items 16 and 17, paragraph 155-5(2)(i) and item 5 of the table in subsection 115-15(1) of Schedule 1 to the TAA 1953]***

1.49 This will ensure that, among other things, the Commissioner can amend the assessment of the major bank levy if necessary and gives an ADI the right to object to the assessment under Part IVC of the TAA 1953 (see section 155-90 of Schedule 1 to the TAA 1953).

1.50 The amount of major bank levy that an ADI is liable to pay for a quarter is due and payable on or before the first day:

- that occurs on or after the MBL reporting day for the quarter; and
- on which the last instalment that the ADI is liable to pay within an instalment quarter is due under the PAYG instalment provisions.

[Treasury Laws Amendment Bill, Schedule 1, item 15, section 115-10 of Schedule 1 to the TAA 1953]

1.51 In this regard, ADIs that are subject to the major bank levy are generally monthly instalment payers for PAYG instalment purposes. Therefore, the major bank levy that is payable for a particular quarter is generally due and payable on or before the 21st day of the third month in the quarter that follows the quarter to which the levy relates.

1.52 However, as a transitional rule, in relation to the major bank levy that an ADI is liable to pay for the quarter ending on 30 September 2017, the due date for payment will be deferred by a quarter. ***[Treasury Laws Amendment Bill, Schedule 1, subitem 23(2)]***

1.53 Therefore, in practical terms, for the 2017-18 income year, the major bank levy will be due and payable on or before the following dates:

- the major bank levy for the quarter ending on 30 September 2017 will be due and payable on or before 21 March 2018;
- the major bank levy for the quarter ending on 31 December 2017 will be due and payable on or before 21 March 2018;
- the major bank levy for the quarter ending on 31 March 2018 will be due and payable on or before 21 June 2018; and
- the major bank levy for the quarter ending on 30 June 2018 will be due and payable on or before 21 September 2018.

1.54 Consequently, an applicable reporting standard will not require an ADI to give APRA a report for the quarter ending on 30 September 2017 until at least January 2018.

1.55 If an amount of major bank levy remains unpaid after it is due and payable, the ADI is liable to pay general interest charge on the unpaid amount for each day in the period that:

- started at the beginning of the day by which the amount was due to be paid; and
- finishes at the end of the last day at the end of which either the amount, or the general interest charge on the amount, remains unpaid.

[Treasury Laws Amendment Bill, Schedule 1, items 14 and 15, item 45A in the table in section 8AAB(4) of the TAA 1953 and section 115-10(2) of Schedule 1 to the TAA 1953]

1.56 Consequential amendments ensure that:

- a liability to pay the major bank levy will be a *tax-related liability*; and

- the Major Bank Levy Act will be a *BAS provision*.

[Treasury Laws Amendment Bill, Schedule 1, items 10 and 18, the definition of 'BAS provisions' in subsection 995-1(1) of the ITAA 1997 and item 136 of the table in subsection 250-10(2) of Schedule 1 to the TAA 1953]

1.57 This will ensure that, among other things, the provisions in the TAA 1953 relating to the collection and recovery of tax related liabilities will apply to the major bank levy.

1.58 A further consequential amendment will ensure that the Commissioner can make binding public, private and oral rulings in relation to the major bank levy. ***[Treasury Laws Amendment Bill, Schedule 1, item 22, paragraph 357-55(fd) of Schedule 1 to the TAA 1953]***

Anti-avoidance law

1.59 A new anti-avoidance law will apply to deter ADI's from entering into schemes to obtain major bank levy benefits (MBL benefits). If the sole or dominant purpose of entering into a scheme is to give an entity an MBL benefit, then the Commissioner may negate the benefit an entity gets from the scheme by making a determination. ***[Treasury Laws Amendment Bill, Schedule 1, item 15, section 117-1 of Schedule 1 to the TAA 1953]***

1.60 The new anti-avoidance law is consistent with other general anti-avoidance provisions in the taxation law. The object of the anti-avoidance law is to deter schemes to give entities benefits that reduce or defer major bank levy liabilities. ***[Treasury Laws Amendment Bill, Schedule 1, item 15, section 117-5 of Schedule 1 to the TAA 1953]***

When does the new anti-avoidance law apply

1.61 The anti-avoidance law applies if:

- an entity gets or got an MBL benefit from a scheme;

- taking into account certain specified matters, it is reasonable to conclude that an entity that (whether alone or with others) entered into or carried out the scheme, or a part of the scheme, did so for the sole or dominant purpose of that entity or another entity getting an MBL benefit from the scheme; and

- the scheme has been entered into at or after 7.30 pm by legal time in the Australian Capital Territory on 9 May 2017, or has been or is carried out or commenced at or after that time (and was not entered into before that time).

[Treasury Laws Amendment Bill, Schedule 1, item 15, subsection 117-10(1) of Schedule 1 to the TAA 1953]

1.62 For the purposes of applying the anti-avoidance law, it does not matter whether the scheme, or any part of the scheme, was entered into or carried out inside or outside Australia. ***[Treasury Laws Amendment Bill, Schedule 1, item 15, subsection 117-10(2) of Schedule 1 to the TAA 1953]***

1.63 An entity gets an ***MBL benefit*** from a scheme if:

- an amount of major bank levy that is payable by an entity (apart from under Division 117 of Schedule 1 to the TAA 1953) is, or could reasonably be expected to be, smaller than it would be apart from the scheme or a part of the scheme — for these purposes, the circumstances in which a liability will be smaller include a case where a liability is zero, or where there is no such liability for a particular quarter; or
- all or part of an amount of major bank levy that is payable by an entity (apart from under Division 117 of Schedule 1 to the TAA 1953) is, or could reasonably be expected to be, payable later than it would have been apart from the scheme or a part of the scheme.

[Treasury Laws Amendment Bill, Schedule 1, items 13 and 15, definition of 'MBL benefit' in subsection 995-1 of the ITAA 1997 and section 117-15 of Schedule 1 to the TAA 1953]

1.64 Matters that can be taken into account in considering an entity's purpose in entering into or carrying out a scheme, or a part of the scheme, are:

- the manner in which the scheme was entered into or carried out;
- the form and substance of the scheme;
- the time at which the scheme was entered into and the length of the period during which the scheme was carried out;
- the effect that the Major Bank Levy Act, and any other taxation law to the extent that it applies in relation to that Act, would have in relation to the scheme (apart from Division 117 of Schedule 1 to the TAA 1953);

- any change in financial position of the entity that has resulted, or may be reasonably expected to result, from the scheme;

- any change that has resulted, or may be reasonably expected to result, from the scheme in the financial position of an entity that is a connected entity — a connected entity is an entity that has or had a connection or dealing with the entity, whether the connection or dealing is or was of a business or other nature;

- any consequences for the entity, or for a connected entity, of the scheme having been entered into or carried out; and

- the nature of the connection (whether of a business or other nature) between the entity and a connected entity.

[Treasury Laws Amendment Bill, Schedule 1, item 15, section 117-20 of Schedule 1 to the TAA 1953]

1.65 The anti-avoidance rule is intended to target schemes that have a sole or dominant purpose of avoiding the major bank levy, including through reducing or delaying the liability to the major bank levy. Similar to Part IVA of the *Income Tax Assessment Act 1936*, the anti-avoidance rule is focused on arrangements, or parts of arrangements, that are artificial or contrived.

1.66 The major bank levy is not intended to prevent an ADI from moving to more stable sources of funding. This anti-avoidance rule will not apply to schemes that have the effect of decreasing, on an ongoing basis, an ADI's applicable liabilities amount to the extent that this reflects a genuine change in the composition of the ADI's funding and activities.

Example 1.2

In complying with other regulatory obligations, an ADI that is liable to pay the major bank levy reduces its short term debt liabilities and increases its Additional Tier 1 Capital on issue. This has the effect of reducing the amount of major bank levy that the ADI is liable to pay.

Having regard to the matters listed in section 117-20 of Schedule 1 to the TAA 1953, this is not likely to be a scheme to which the anti-avoidance rule applies:

- the manner in which the scheme was entered into — in this case, the change to the bank's funding mix has been implemented in a straightforward way by raising Additional Tier 1 Capital consistent with its regulatory requirements and using the proceeds to retire short-term debt;

- the form and substance of the scheme — in this case, the substantive effect of the change is to increase the bank's reliance on stable funding sources and puts the bank in a stronger prudential position (substance follows form);
- the time at which the scheme was entered into and the length of the period during which the scheme was carried out — this matter looks at whether the scheme operates around the end of a quarter, and the duration of the scheme itself. In this case, the change to the bank's funding mix is long term (that is, the change is not made to achieve a temporary effect); and
- any change in financial position of the entity — in this case, the ADI has effected a real change in its financial position through making itself less reliant on short term funding and increasing its Additional Tier 1 Capital on issue.

1.67 Similarly, the major bank levy is not intended to prevent an ADI from reducing its liabilities where there has been a reduction in its funding needs. For example, the anti-avoidance provisions are not intended to apply to the permanent repayment of a loan asset in the ordinary course of business, with the effect that any associated funding has been repaid or any associated derivative liability has been closed out.

1.68 Types of arrangements that could potentially be subject to the anti-avoidance rule include those that involve:

- temporary reductions in liabilities before the end of a quarter that have the effect of reducing liability to the major bank levy which are not explicable by the ordinary operations of the ADI — for example:
  - an arrangement whereby, on request from the ADI, a customer changes the form of its monies held with the ADI over a quarter end with the effect of decreasing its applicable liabilities amount where, in compensation for the temporary change, the bank pays the customer a fee or offers other services at a below market rate;
  - an arrangement that has the effect of 'bed and breakfasting' liabilities with a related party over a quarter end; and
  - an arrangement that has the effect of 'window dressing' to achieve a temporary effect over a quarter end.

- permanent reductions in liabilities that do not involve any substantive change in the activities or risks of the ADI — for example, an arrangement where a loan asset and funding liability is shifted to a subsidiary and the risk and benefits brought back to the ADI through the use of derivatives, with the effect that there is no significant change in the activities that the ADI performs or the risks that it is exposed to, but there is a permanent reduction in the liabilities of the ADI.

Consequences that arise when the new anti-avoidance law applies

1.69 For the purpose of negating an MBL benefit an entity gets or got from a scheme, the Commissioner may:

- make a determination stating the amount that is (and has been at all times) the entity's major bank levy liability for a specified quarter that has ended; or

- make a determination stating the amount that is (and has been at all times) a particular amount of a liability that is relevant to working out the applicable liabilities amount for a specified quarter that has ended.

[Treasury Laws Amendment Bill, Schedule 1, item 15, subsection 117-25(1) of Schedule 1 to the TAA 1953]

1.70 The determination is not a legislative instrument. ***[Treasury Laws Amendment Bill, Schedule 1, item 15, subsection 117-25(2) of Schedule 1 to the TAA 1953]***

1.71 The Commissioner may take such action as the Commissioner considers necessary to give effect to the determination. ***[Treasury Laws Amendment Bill, Schedule 1, item 15, subsection 117-25(3) of Schedule 1 to the TAA 1953]***

1.72 For the purpose of making an assessment, a statement in a determination made for these purposes has effect according to its terms, despite any other provisions in a taxation law. ***[Treasury Laws Amendment Bill, Schedule 1, item 15, section 117-30 of Schedule 1 to the TAA 1953]***

1.73 For the purposes of making the determination, the Commissioner may:

- treat a particular event that actually happened as not having happened;

- treat a particular event that did not actually happen as having happened and, if appropriate, treat the event as having happened at a particular time and having involved particular action by a particular entity; and

- treat a particular event that actually happened as having happened at a different time from the time it actually happened or having involved particular action by a particular entity (whether or not the event actually involved any action by that entity).

[Treasury Laws Amendment Bill, Schedule 1, item 15, section 117-35 of Schedule 1 to the TAA 1953]

1.74 To avoid doubt, statements relating to different quarters and different MBL benefits may be included in a single determination. ***[Treasury Laws Amendment Bill, Schedule 1, item 15, section 117-40 of Schedule 1 to the TAA 1953]***

1.75 The Commissioner must give a copy of a determination to the entity whose liability for major bank levy is stated in the determination. However, a failure to comply with this requirement does not affect the validity of the determination. ***[Treasury Laws Amendment Bill, Schedule 1, item 15, section 117-45 of Schedule 1 to the TAA 1953]***

1.76 If the Commissioner makes a determination for the purpose of negating an MBL benefit, the entity may be liable to an administrative penalty, consistent with the administrative penalties that apply in other circumstances when an entity enters into a scheme, the effect of which is negated because of an anti-avoidance law (subparagraph 284-145(1)(b)(i) of Schedule 1 to the TAA 1953).

1.77 If an ADI to whom a determination relates is dissatisfied with the determination, the ADI may object against it in the manner set out in Part IVC of the TAA 1953. ***[Treasury Laws Amendment Bill, Schedule 1, item 15, section 117-50 of Schedule 1 to the TAA 1953]***

Exchange of information between the Commissioner and APRA

1.78 The provisions in the tax law relating to the confidentiality of taxpayer information are being amended so that it is not an offence for the Commissioner to give information to APRA for the purposes of administering the major bank levy. ***[Treasury Laws Amendment Bill, Schedule 1, item 19, item 6 of the table in subsection 355-65(3) of Schedule 1 to the TAA 1953]***

1.79 Similarly, the APRA Act is being amended so that it is not an offence for APRA to give information to the Commissioner in relation to the major bank levy. ***[Treasury Laws Amendment Bill, Schedule 1, item 1, subsection 56(5D) of the APRA Act]***

Application and transitional provisions

1.80 The Major Bank Levy Act will apply from and commence on the day after the Act receives Royal Assent. ***[Major Bank Levy Bill, section 2 of the Major Bank Levy Act]***

1.81 The amendments to the APRA Act and the Collection of Data Act apply from the commencement of the Major Bank Levy Act. ***[Treasury Laws Amendment Bill, item 2 of the table in subsection 2(1)]***

1.82 The amendments to the ITAA 1997 and the TAA 1953 major bank levy will apply in relation to quarters starting on or after 1 July 2017, and commence from the commencement of the Major Bank Levy Act. ***[Treasury Laws Amendment Bill, item 3 of the table in subsection 2(1); Schedule 1, item 23]***

STATEMENT OF COMPATIBILITY WITH HUMAN RIGHTS

Prepared in accordance with Part 3 of the *Human Rights (Parliamentary Scrutiny) Act 2011*

Major Bank Levy Bill 2017
Treasury Laws Amendment (Major Bank Levy) Bill 2017

1.83 These Bills are compatible with the human rights and freedoms recognised or declared in the international instruments listed in section 3 of the *Human Rights (Parliamentary Scrutiny) Act 2011*.

Overview

1.84 The Major Bank Levy Bill will introduce a levy on ADIs with total liabilities of greater than $100 billion. The levy is imposed at a rate of 0.015 per cent on certain liabilities of the ADI that are reported to APRA on a quarterly basis under a reporting standard.

1.85 Schedule 1 to the Treasury Laws Amendment Bill amends the APRA Act, the Collection of Data Act, the ITAA 1997 and the TAA 1953 to specify certain administrative features relating to the major bank levy, including the requirement that the levy is payable to the Commissioner quarterly.

Human rights implications

1.86 These Bills do not engage any of the applicable rights or freedoms.

Conclusion

1.87 These Bills are compatible with human rights as they do does not raise any human rights issues.

Chapter 2
Regulation impact statement

1. The problem

2.1 Failing to ensure Australia is on a sustainable fiscal path will put at risk future growth, reducing opportunities for better paying jobs, and burdening future generations with debt.

2.2 Delaying action will make it more difficult to guarantee the essential services that Australians rely on. An improved structural fiscal position will place Australia in a better position to withstand any future economic downturns, including dealing with shocks such as those seen in the global financial crisis.

2.3 In developing possible policy options to meet this policy problem, the Government has also sought to address a range of long term policy objectives that the Government is working towards in the banking sector:

- ensuring the banking sector makes a fair contribution to the economy given its unique role in Australia's economy and the associated systemic risks that it imposes;
- improving competition and accountability; and
- complementing prudential reforms.

2. Case for government action/objective of reform

2.4 The Government is taking action, as part of the 2017-18 Budget, to charge a levy on ADIs with liabilities greater than $100 billion. Reflecting the current structure of the banking industry, this levy can be expected to apply to just five ADIs: ANZ, Commonwealth Bank of Australia, National Australia Bank, Westpac and Macquarie bank (hereon referred to as 'the major banks').

2.5 The levy will raise around $1.5 billion per year over the next four years and will be contribute to budget repair over the forward estimates period. The levy will also contribute to strengthening the structural position of the budget for the long term — providing greater fiscal capacity to deal with shocks such as those seen in the global financial crisis.

2.6 The revenue estimates are based on data sourced from APRA, uplifted for credit growth over the forward estimates. They take account of interactions with other taxes — most notably corporate income tax — and the timing of payments associated with those taxes, as well as dividend and franking credit interactions and other relevant factors.

2.7 Repairing the budget and maintaining the Australian Government's AAA credit rating will also benefit the largest banks, as their credit ratings, and hence funding costs, are more closely linked to the Government's credit rating.

2.8 In addition to the bank levy contributing in the shorter term to budget repair and to strengthening the structural fiscal position for the long term, it will have a number of other beneficial impacts related to ongoing stability and competition settings, notably:

- ensuring a fair contribution from major banks to the economy given risks to the economy arising from large leveraged banks;
- providing a more level playing field for smaller banks and non-bank competitors; and
- complementing broader prudential reforms being implemented by APRA and the Government.

2.9 The levy will also bring Australia's taxation arrangements for ADIs into alignment with other advanced countries.

A fair contribution from major banks to the community

2.10 The major Australian banks are amongst the most profitable banks in the advanced world. Rates of return on equity of Australia's largest banks have averaged around 15 per cent over the past five years, far exceeding those in the United States, Europe and Japan, and matched only by Canadian banks.

2.11 Over the past year, the five banks that will be affected by the levy have collectively earned more than $30 billion in profit after tax.

2.12 The global financial crisis demonstrated that large, leveraged banks are a major source of systemic risk. If one or more of Australia's major banks became distressed or was seen to be at risk of failing, there would be significant contagion to other financial institutions.

2.13 This would impose large costs on Australia's financial system and economy. The cost of borrowing would rise, with significant flow-on effects to mortgage holders, businesses and government finances. Credit supply could also be disrupted, starving the economy of the capital needed for it to grow and create jobs. In essence, the levy represents a fair additional contribution from the largest banks for the risks they pose to the financial system and economy.

Provide a more level playing field for smaller banks and non-bank competitors

2.14 The major banks represent 80 per cent of the bank deposit market, 80 per cent of all credit provided by banks and around three-quarters of the credit card market.

2.15 The House of Representatives Committee on Economics' Review of the four major banks (the Coleman Report) found these major banks' size and market dominance affords them significant funding cost advantages and pricing power at the expense of their customers. This contributes to their ongoing dominance of the market for consumer and business lending.

2.16 The imposition of the levy will reduce the largest banks' funding cost advantage and contribute to a more level playing field. This will enhance the ability of smaller banks and non-bank lenders to compete more aggressively with the largest banks. Several smaller banks have expressed their support for the levy.

Complement prudential reforms being implemented by APRA and the Government

2.17 Consistent with its response to the Financial System Inquiry, the Government and APRA remain committed to a range of reforms to strengthen the resilience of the Australian financial system.

2.18 These reforms include:

- setting bank capital levels such that they are 'unquestionably strong';
- strengthening APRA's crisis management powers; and
- ensuring our banks have appropriate loss absorbing capacity.

2.19 The design of the levy complements the 'unquestionably strong' direction of prudential policy. The levy will not apply to common equity and Additional Tier 1 (AT1) capital (capital instruments that can be converted to equity or be written off in the event of distress). APRA has confirmed that the payment of the levy will not have a material impact on the resilience of the banking system and that the levy regime does not harm its prudential policy objectives.

2.20 As the levy excludes deposits protected by the Financial Claims Scheme (FCS), it also creates an additional incentive for affected banks to move towards more stable, deposit-based funding. In doing so, it complements prudential measures aimed at making banks more resilient to market disruptions of the sort seen in the global financial crisis.

3. Policy options

2.21 Three policy options have been identified.

- Option 1: No major bank levy.
- Option 2: Major bank levy (as outlined in the 2017-18 Budget measure).
- Option 3: Major bank levy (with amendments identified in post-Budget consultation).

Option 1: No major bank levy

2.22 The first option is to not impose a major bank levy.

Option 2: Major bank levy (as outlined in the 2017-18 Budget measure)

2.23 In the 2017-18 Budget, the Government announced the introduction of a levy on ADIs with liabilities of at least $100 billion (the major bank levy), raising approximately $1.5 billion per year and assisting with Budget repair.

2.24 The key design features of this option are outlined in Table 2.1.

Table 2.1: Key design features of Option 2

Application	ADIs with liabilities greater than $100 billion.
Levy rate	The levy would be calculated quarterly as 0.015 per cent of the levy base at the end of each quarter (six basis points on an annual basis).
Levy base	Liabilities subject to the levy would, for example comprise non-FCS protected deposits, wholesale funding liabilities (for example: senior debt (corporate bonds); commercial paper; certificates of deposit; and Tier 2 capital instruments) and other liabilities. The following liabilities would be excluded: • AT1 capital and deposits protected by the FCS. • Together these exclusions would account for around 25 per cent of an ADI's liabilities on average. Applying the levy to around 75 per cent of major banks' liabilities has three advantages: it ensures that the levy is simple; reduces integrity risks; and minimises Australian Taxation Office (ATO) administration and ADI compliance costs by relying on data already reported to APRA.
Administered	ATO
Non-banking business	Liabilities of a bank's overseas and non-bank subsidiaries would not be included with the bank's licensed entity liabilities to which the levy would apply. Therefore a banking group's non-bank businesses — insurance and superannuation — would not be subject to the levy. But its offshore bank branches (that are not a separate legal entity and are typically used to raise offshore wholesale debt) would be.
Revenue raised	The levy would raise $6.2 billion, net of interactions with other taxes (including corporate income tax), over the forward estimates period.

Option 3: Major bank levy (with amendments identified in post-Budget consultation)

2.25 Option 3 is to impose a major bank levy — where the broad parameters of the levy remain similar to Option 2 — but with amendments that address certain issues raised during the consultation process. The most important of these are highlighted in the key design features outlined in Table 2.2.

Table 2.2: Key design features of Option 3

Application	As per Option 2
Levy rate	The levy rate remains as per Option 2, but some components of total liabilities are calculated on the basis of a quarterly average rather than the value at quarter-end. • While a single point of time calculation point is less complex, it risks market disruptions as it increases the incentives to minimise liabilities (especially short-term liabilities) at the end of each quarter.
Levy base	As per Option 2, but with the following changes. • In calculating the levy base, derivatives would be included on a net basis (that is derivative liabilities less derivative assets), with a minimum value of zero. • The quarterly average value of Exchange Settlement Account balances held with the RBA would be deducted. This would insulate the payments system and monetary policy from risks that balances will be reduced to lower levy payments. This deduction would only have a negligible effect on estimated revenue from the levy.
Administered	As per Option 2
Non-banking business	As per Option 2
Revenue raised	As per Option 2, with the following changes. • Each quarterly levy instalment would be payable in totality in the final month of each quarter, rather than in monthly instalments. This addresses administrative complexities raised during the consultation process. This would have no effect on the revenue forecasts. • The due date for payment of the first quarterly instalment of the levy would be delayed until March 2018, providing the banks with additional time to upgrade their systems for the purposes of the levy.

4. Cost benefit analysis of each option/Impact analysis

2.26 The key stakeholders impacted by the levy are the five major banks who currently have liabilities greater than $100 billion. The risk that the major banks may seek to pass on the costs of the levy to customers is discussed in the section on the economic impact of the levy.

2.27 Both Options 2 and 3 were developed in accordance with standard budget processes for revenue measures of this scope and scale. Consistent with the *Charter of Budget Honesty Act 1998* and the *Charter of Budget Honesty Policy Costings Guidelines* (as updated in 2016) second-round or economy wide modelling was not included in the modelling of the major bank levy. In light of this and mindful of the limitations of modelling techniques, second round effects are rarely included in costings for a range of reasons, including uncertainty in estimating the magnitude and timing of the effects, and because second-round effects are likely to be small relative to the direct financial impact of the measure. Where second-round effects have been included in costings, it is mainly for broad based packages such as the *2000 New Tax System* which introduced the goods and services tax.

2.28 In examining possible design options for the levy, consideration was given to different approaches, for example, a levy on assets. It was assessed however that the appropriate base for applying the levy was the liability side of the balance sheet. This aligns with the approach taken in the majority of countries that apply some form of bank levy (refer to Table 2.3). It is also in accordance with the International Monetary Fund's 2010 *A Fair and Substantial Contribution by the Financial Sector* report to the G-20 that a broad based levy on the liability side of the balance sheet (with appropriate exclusions, such as equity) is the preferred option. A broad based levy allows for a lower rate for any given amount of revenue, limiting the risk of unintended distortion.[1]

Option 1: No major bank levy

2.29 This option would have zero regulatory cost, but would also not contribute to the policy goal of budget repair and would not provide greater fiscal capacity to deal with shocks such as seen in the global financial crisis.

Option 2: Major bank levy (as outlined in the 2017-18 Budget measure)

2.30 By taking advantage of existing reporting and payment processes, Option 2 would have limited regulatory costs. All data required to calculate the levy is already reported to APRA or otherwise generated for other reporting purposes such as annual reports.

2.31 It is estimated that the small regulatory adjustments required would have a total cost of $10,000 over a 10 year period.

2.32 While Option 2 is administratively simple and likely to have lower regulatory costs, it potentially has other costs based on its design

[1] International Monetary Fund, *A Fair and Substantial Contribution by the Financial Sector*, Final Report for the G-20, June 2010

features that may be significant but are difficult to quantify. These include:

- possible impacts on the functioning of Australia's capital markets, particularly short-term money and repo markets where many securities mature overnight and trade with limited margins. In designing Option 2 these risks had been identified and were a focus for consultation. Those consultations suggested that these risks could be more significant in Australia than the initial assessment.
  – Trade in these markets underpins the liquidity of Australia's financial system. The imposition of a 0.015 per cent levy on short-term funding securities that each major bank holds on a single day at quarter end would likely make a significant portion of these positions less profitable at that time. This could see major banks avoid entering into new liabilities and attempting to close out existing liabilities towards the end of each quarter.
  – Concerns were raised that if this happened it would have the potential to disrupt short term funding markets, impairing their functioning, and have adverse implications for the RBA's day-to-day operations and liquidity management.
- possible impacts of this option on the balances held by the major banks in the Exchange Settlement Account with the RBA. In particular, a levy on these balances would create an incentive for banks to reduce their balances as it would make holding them unprofitable. A reduction in Exchange Settlement Account balances could:
  – reduce liquidity in the inter-bank cash market, an important market for the purposes of conducting monetary policy; and
  – create risk of payment failure if a large transaction occurred overnight or on the weekend.

Option 3: Major bank levy (with amendments identified in post-Budget consultation)

2.33 Option 3 includes a number of amendments that address some of the potential non-regulatory costs identified in relation to Option 2. This results in some increase in regulatory costs and complexity, although these remain modest.

2.34 Option 3 would involve APRA creating a new reporting form to collect the data required to calculate the levy. This form would require the major banks to report:

- some existing data provided to APRA; and
- some new data (for example, the quarterly average value of wholesale funding liabilities balances).

2.35 While this will impose some additional compliance costs compared to Option 2, banks already collect much of the additional data required for internal liquidity management and statutory reporting purposes as well as for APRA's liquidity forms, and it is not expected that these costs would be significant (although the APRA data are currently collected on a different consolidation basis). Compliance costs would also be reduced by delaying the collection of the data for the levy until January 2018, thereby giving the major banks additional time to build infrastructure to report this data.

2.36 While the number of new data items to be collected is small and relate to core banking data, it is expected that affected banks will need to undertake system upgrades to allow for new calculations to be performed on this data for the purposes of calculating the levy (that is, a quarterly average figure for wholesale funding liabilities).

2.37 While the scale and cost of these upgrades is likely to vary between the banks depending on their current systems — making it difficult to estimate the precise cost — industry feedback (based on certain assumptions) suggests the additional work required would, on average, cost in the order of $3 million per bank, and would cover:

- the development of enhanced automated reporting, including sourcing of data and testing;
- ensuring controls are in place for relevant inputs and outputs, such as cross-validations to other returns and reports and monthly analytical reviews;
- ensuring that intercompany balancing remains effective on a quarterly basis for regulatory reports (as they are used as the basis of calculation);
- the development of executive review and sign off protocols given the size and sensitivity of the payment; and

- extending current assurance processes (across the finance, risk, treasury and tax functions and external audit) to cover the review of inputs, calculation and payment.

2.38 The majority of these costs would be upfront and the ongoing compliance cost is expected to be manageable.

2.39 This would suggest a total cost of $15 million, or $1.5 million per annum, across the major banks over a ten year period.

2.40 This appears broadly in line with previous experiences with new data collection requirements for APRA-regulated entities. Examples of previous, and more extensive, data collection changes include:

- introduction of new reporting standards applying to trustees of registrable superannuation entities (RSE licensees) as part of the 'Stronger Super reforms'. In the Regulation Impact Statement for this measure (OBPR ID: 14624), industry submissions on the cost to implement options (which envisaged up to 36 new reporting standards being applied to RSE licensees) included estimates from $2 million up to $8 million per RSE licensee for the information technology setup costs; and

- on the proposal for the net stable funding ratio (NSFR) for the banking system, the Regulation Impact Statement (OBPR ID: 2015/19640) estimated costs associated with systems modifications (depending on existing internal information technology systems), staffing costs to perform tasks associated with the NSFR and the associated reporting costs through providing regular reports to APRA for NSFR purposes of approximately $24 million for 15 ADIs over 10 years, or $2.4 million per year in total.[2]

2.41 Option 3 also significantly reduces the non-quantifiable costs of the major bank levy that were raised in relation to the Option 2 levy. The most important of these relate to short-term liabilities and Exchange Settlement Account balances:

- shifting to a quarterly average basis for calculating the levy on wholesale funding liabilities, thereby reducing incentives for banks to adjust liability holdings at specific points in time (such as towards the end of each quarter). Applying the levy

[2] This costing was for option 1, which was to only apply the Basel NSFR standard to larger ADIs.

across all wholesale funding liabilities held during the quarter will avoid creating incentives for the major banks to withdraw from their market making function at quarter end; and

- deducting an amount equal to the quarterly average value of their Exchange Settlement Account balances for each quarter from the levy base broadly insulates the payments system and monetary policy from the impact of the levy, with only marginal expected effects on revenue and regulatory burden.

Considerations on the economic impact of the levy

2.42 The economic impact of the levy will depend upon the extent to which it affects bank borrowers, lenders, shareholders or some combination of these groups.

2.43 It is not possible to be unequivocal as to the ultimate incidence of the levy — it can be passed through to those the banks lend to (in respect of residential mortgages, business lending and personal credit), deal with or provide services to, or their non-equity funding sources (wholesale capital markets, depositors) or be borne by the banks themselves (through reduced profits, or via increased efficiency or other cost-cutting measures).

2.44 The degree of competition in different market segments will be a key determinant of the ability of the major banks to pass on the costs of the levy. Other regulatory and tax settings, major banks' perceptions of constraints on their pricing decisions, as well as the general domestic and global economic environment, will also determine the incidence of the levy. Incidence is also likely to vary over time — in the long-run, competitive forces are likely to be more of a constraint than in the short-run.

2.45 The Australian Competition and Consumer Commission has been given the role to monitor and report on interest rates and other charges imposed by affected banks in relation to residential mortgage products following the introduction of the levy, with the aim of ensuring that customers are not unduly impacted. This will provide customers with an independent source of information that will be helpful in informing any decision to switch to another ADI if they are dissatisfied with how their bank has responded to the introduction of the levy.

2.46 In the extreme case that the costs of the levy were to be fully passed on to bank customers, lending rates faced by major bank borrowers would increase, although the major banks may be unable to pass the cost onto all assets — for example, banks may not be able to increase the yields of their high-quality liquid asset holdings. On this basis, and though the six basis point levy is applied to around 75 per cent of bank liabilities, the overall impact on major bank loan interest rates or fees would be around six basis points.

2.47 The economy-wide impact would however be smaller. The affected banks currently account for around 80 per cent of bank credit extended in the economy, but bank credit itself only accounts for about 80 per cent of economy-wide borrowing. As such, the economy-wide impact on borrowing costs overall would likely be closer to four basis points.

2.48 To the extent that affected banks did raise their lending rates, this could lead to some migration of lending to non-affected banks, which would also lessen the impact on economy-wide lending rates.

2.49 For completeness, Treasury modelled the economy-wide effects of the proposed bank levy. This required making various assumptions with respect to the incidence of the levy, though sensitivity analysis showed that overall the results were invariant to those assumptions. This affirmed our view that the impact is expected to be negligible

2.50 Finally, when setting cash rates the RBA takes into account, among other things, the actual lending rates faced by households and businesses. When the RBA changes the cash rate it normally does so 25 basis point increments, which typically flow through in full to borrowing rates. The impact of a single RBA rate 25 basis point increase would far outweigh any possible impact on borrowing costs of a six basis point levy.

2.51 Although there may be differences in the impact on the economy depending on whether the levy is passed on to other groups (such as depositors and shareholders) or there is a greater focus on internal efficiencies and improved productivity, or some combination of these, the absolute size of the levy is less than one-tenth of a percentage point of GDP. This means it is unlikely to have an impact on the economy above usual material reporting thresholds.

Overseas bank levies

2.52 A number of foreign jurisdictions have introduced bank levies that are similar in design to the major bank levy (see Table 2.3).

Table 2.3: International Bank Levies

Jurisdiction (introduced)	***Levy base***	***Levy rate***	***Exemptions & threshold***
Australia (proposed 2017)	Liabilities	0.06% (annualised)	Deposits protected by the FCS, AT1 capital before deductions, derivatives Threshold: $100bn
Austria (2011)	Liabilities	<€20bn: 0.09% >€20bn: 0.11%	Insured deposits Threshold: €1bn
Belgium (2012)	Liabilities	0.13231% (2016)	Levied on 'debt towards clients'
France (2011)	Minimum regulatory capital	0.5%	Threshold: €500m
Germany (2011)	Liabilities Derivatives	Liabilities: >€300m: 0.02% progressively increasing to >€300bn: 0.06% Derivatives: 0.0003%	Retail deposits, certain reserves, certain profit participation rights Threshold: €300m Maximum: 20% of annual earnings Minimum: 5% of calculated annual contribution
Hungary (2010)	Assets	<HUF50bn: 0.15% >HUF50bn: 0.24%	Interbank loans
Iceland (2011)	Total liabilities	0.376%	Threshold: ISK50mn
Netherlands (2012)	Liabilities	Long-term: 0.022% Short-term: 0.044%	Protected deposits, regulatory capital, insurance liabilities Threshold: €20bn
Poland (2016)	Assets	0.44%	Equity capital and government securities Threshold: PLN4bn
Portugal (2011)	Liabilities	0.01-0.11%	Tier 1 and 2 capital, and protected deposits

Jurisdiction (introduced)	***Levy base***	***Levy rate***	***Exemptions & threshold***
Slovakia (2012)	Liabilities	0.2%	'Own funds' and subordinated debt
Sweden (2009)	Liabilities	0.09%	Protected deposits
United Kingdom (2011)	Liabilities	Long-term and equity: 0.09% (0.05% from 2021) Short-term: 0.18% (0.1% from 2021)	Protected deposits, Tier 1 capital, sovereign repos, other selected liabilities

2.53 These bank balance sheet levies commonly adopt a liabilities base rather than other options such as assets or regulatory capital. Consideration of their design, in particular that of the United Kingdom, has reinforced the value of adopting a broad base/low rate approach that limits exclusions from total liabilities in setting the base.

2.54 Given their recent introduction, there is limited empirical evidence on the incidence and impact of bank levies introduced in other countries (for a summary, see Table 2.4).

2.55 The incidence of bank levies may be passed on to customers (in the form of higher interest rates on loans) although the evidence suggests this is not universal and is likely to depend in part on country-specific factors. Given the relatively small increases in lending rates that may be associated with the introduction of a bank levy, very few studies have considered possible economic impacts — those that have conclude that the economic impacts are not likely to be material. Australia's levy has been designed to complement prudential reforms, and there is some evidence to suggest that bank levies can promote financial stability — levies introduced in Europe have been found to have induced large increases in bank capital levels, due to the levies increasing the cost of wholesale funding relative to equity.

Table 2.4: Existing evidence on the incidence and impact of bank levies

Study *Countries studied*	*Impact on lending / deposit rates*	*Impact on economy*	*Impact on capital / leverage / risk*	*Notes*
Devereux et al. (2013) ***Cross-country study (EU levies)***	—	—	Banks reduced their leverage, but less well-capitalised banks also increased risk taking (on the asset side)	—
Kogler (2015) ***Cross-country study (EU levies)***	Lending rates and net interest margins increased moderately, and by more in concentrated and poorly capitalised markets. Deposit rates unaffected.	Moderate increases in lending rates not suggestive of large economic impact	—	—
Deutsche Bundesbank (2014) ***Germany***	Affected banks reduced their lending and increased deposit rates. No significant change in lending rates.	—	—	—
Buch et al (2016) ***Germany***	Affected banks reduced lending and increased new deposit rates, particularly non-household deposits.	No significant impact on macro-economy*	—	This paper is a peer-reviewed extension of Bundesbank (2014)

Study ***Countries studied***	***Impact on lending / deposit rates***	***Impact on economy***	***Impact on capital / leverage / risk***	***Notes***
Capelle-Blancard and Havrylchyk (2013) ***Hungary***	Banks shift the tax burden to customers by raising interest and fee margins for borrowers with outstanding loans (rather than new loans).	—		—

***This finding was raised in an online column by the authors in March 2017*. See: http://voxeu.org/article/assessing-effects-regulatory-bank-levies**

5. Consultation

2.56 A targeted consultation approach has been adopted following the announcement of the levy in the 2017-18 Budget to reflect the small number of directly affected stakeholders. This targeted consultation has been effective in identifying issues in levy design, reflected in the changes between Options 2 and 3, even though the ordinary practice of a 30 day consultation period has not been possible because of the Government's intention to introduce the legislation ahead of the commencement date of 1 July 2017.

2.57 The levy was considered by the Expenditure Review Committee and Budget Cabinet as part of normal Budget processes and timelines, based on a submission from the Treasurer. In accordance with standard practice, the Department of Finance and the Department of the Prime Minister and Cabinet had the opportunity to comment on that submission.

2.58 While major banks were consulted in confidence some weeks before Budget on proposed changes to APRA's powers that were also announced in the 2017-18 Budget, the market sensitivity of the major bank levy precluded such consultation pre-Budget. As a matter of courtesy, the Chief Executive Officers of the five major banks were informed of the levy just prior to public release of the Budget, but after markets closed.

2.59 A number of issues were identified as part of the consultation process and have been taken into account in Option 3.

2.60 Prior to the announcement in the 2017-18 Budget, Treasury engaged in discussions with APRA, the ATO and the Australian Office of Financial Management on issues associated with the levy and the availability of data. The RBA was also informed and given the opportunity to comment. Discussions also took place with Her Majesty's Treasury in the United Kingdom to understand the design, operation and impact of the United Kingdom's bank levy.

2.61 Subsequent to the announcement of the levy in the 2017-18 Budget, Treasury consulted with the five major banks impacted by the levy and the Australian Bankers' Association. Treasury has received written submissions on the proposed levy from the five major banks and the Australian Bankers' Association as part of its consultation.

2.62 Further consultation was also undertaken with APRA, the Australian Government Solicitor, the RBA, the Australian Securities and Investment Commission, the ATO and the Australian Office of Financial Management.

2.63 Consultation with stakeholders has focused on testing the assumptions underlying the design of the levy to ensure that it meets its policy objectives, with appropriate consideration of compliance costs and impact on APRA's objectives for prudential regulation and the RBA's conduct of monetary policy.

2.64 This consultation process led to changes in the design features of the major bank levy that are reflected in Option 3.

2.65 Further, the major banks, as well as a number of smaller banks that are currently not expected to be impacted by the levy, were given the opportunity to comment in confidence on the draft legislation prior to its finalisation. Two banks also provided comments on additional regulatory compliance costs that may arise in providing additional data for the purposes of the calculation of the levy base under the revised design.

2.66 The comments received on the draft legislation have not required major changes to the design of the levy. This reflects the changes to design that were made between Option 2 and 3 to incorporate the concerns raised during the first round of consultation.

6. Option selection/Conclusion

2.67 The consultation process identified a number of areas that required refinement in relation to the imposition of a major bank levy. These, however, do not undermine the rationale for a levy.

2.68 On this basis, the imposition of a modified levy on the major banks as outlined in Option 3 is the preferred option. Option 3 balances the objectives of the levy, while retaining a low rate and broad base. It also remains relatively simple to administer with low compliance costs while guarding against any financial market disruption risks.

7. Implementation and evaluation/review

2.69 The levy will be introduced via the Major Bank Levy Bill 2017 and the Treasury Laws Amendment (Major Bank Levy) Bill 2017, to be introduced in the Winter 2017 sittings of Parliament.

2.70 A general anti-avoidance rule is included in the legislation to deter the entering into of artificial arrangements with the sole or dominant purpose of reducing the amount of levy they pay. This rule is designed to target artificial arrangements, but would not stop banks from reducing their debt funding (the levy base) and increasing their equity funding.

2.71 Treasury will monitor the impact of the levy on the financial system more broadly as part of its general monitoring activities.

2.72 The Australian Competition and Consumer Commission will undertake a residential mortgage pricing inquiry until 30 June 2018. As part of this inquiry, the Australian Competition and Consumer Commission is able to require relevant ADIs to explain changes or proposed changes to residential mortgage pricing, including changes to fees, charges, or interest rates by those ADIs.

8. References

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