# FINANCIAL SECTOR LEVIES REVIEW

# DISCUSSION PAPER ON POSSIBLE IMPACTS OF AMENDED LEVY DETERMINATION FRAMEWORK ON LEVIES FROM 2005-06

TREASURY
AUSTRALIAN PRUDENTIAL REGULATION AUTHORITY

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## Contents

# BACKGROUND

1. On 7 May 2004 the (then) Minister for Revenue and Assistant Treasurer, Senator the Hon Helen Coonan, released the Report of the Review of Financial Sector Levies and the Government's response to the report. The Government's response indicated its intention to implement 17 recommendations relating to the framework for calculating the financial sector levies, a number of which required legislation. It also stated its intention that the new levy arrangements take effect in time to be implemented for the 2005-06 financial sector levies.

2. A package of legislative changes to give effect to the Government's response to the review was introduced in the House of Representatives on 9 December 2004, passed by the House and Senate two months later and received Royal Assent on 22 February 2005. (The package had been introduced originally on 12 August 2004, but lapsed when Parliament rose for the election.)

3. The seven new Acts that have amended the levy determination framework are the *Superannuation Supervisory Levy Imposition Amendment Act 2005*, the *Financial Institutions Supervisory Levies Collection Amendment Act 2005*, the *Authorised Non-operating Holding Companies Supervisory Levy Imposition Amendment Act 2005*, the *Authorised Deposit-taking Institutions Supervisory Levy Imposition Amendment Act 2005*, the *General Insurance Supervisory Levy Imposition Amendment Act 2005*, the *Life Insurance Supervisory Levy Imposition Amendment Act 2005* and the *Retirement Savings Account Providers Supervisory Levy Imposition Amendment Act 2005*.

4. The amended legislative framework separates the supervisory levies into two components. In addition, it changes the statutory upper limit applying to the restricted component of each levy for the 2005-06 financial year. The calculation of the indexation factor used to establish the statutory upper limits applying in later years is also altered in a way that allows the statutory upper limit to increase by three percentage points annually in excess of movements in the Consumer Price Index.

5. The first, or restricted, component in the new levy structure has a cost-of-supervision based rationale and is structured as a percentage rate on assets subject to minimum and maximum amounts. This structure is the same as that which applied under the old levy framework where the levy determinations were based solely on the cost of supervision.

6. The second, and new, unrestricted levy component has a system impact and vertical equity rationale and is structured as a low percentage rate on assets, without a minimum or maximum amount for individual regulated entities.

# STRUCTURE OF THIS DISCUSSION PAPER

7. This discussion paper provides details on the potential impacts of the new financial sector levy framework on each industry sector and institution regulated by the Australian Prudential Regulation Authority (APRA). The paper is aimed at providing information to industry to facilitate further discussion as input into the determination process that will be completed in the second quarter of 2005.

8. The main changes in the distribution of the financial sector levies among regulated institutions will result from the implementation of recommendations 5 to 10, so most of the analysis in the paper concentrates on these recommendations. Most of the remaining recommendations confirm the continuing appropriateness of key elements used in the previous method of levy determination and, as they will have little or no impact on changes in the financial sector levies, do not receive as much prominence. A complete list of the recommendations accepted by the Government is at Attachment A.

9. This paper is the first step in the consultative process leading to the determination of the 2005-06 levies. As such, it approximately follows the format of previous annual consultation documents for levy determinations and concentrates on the impacts of the review recommendations on levies for that year. However, as the new levy system will apply beyond 2005-06, similar changes also will affect the setting of levies in future years.

10. It should be noted that data used in this paper are those currently available. The final results may vary as updated data become available prior to the final determinations.

## SUMMARY OF SIGNIFICANT CHANGES

11. This section gives a brief overview of the main impacts on the distribution of the levies among the various prudentially regulated entities. The rest of this paper goes into more detail on the data and assumptions used to calculate the possible scenario under the new levy-setting framework that is summarised here.

12. As outlined in the Report of the Review of Financial Sector Levies, the result of the new levy determination framework will be a wider spread of levy charges, with an easing of the levy burden for medium-sized entities and a heavier burden for the largest entities. The Government's response to the review noted that the smallest entities should be no worse off than under the old levy determination methodology.

13. The primary reason for large entities paying a greater proportion and medium-sized entities a smaller proportion of the levies is the introduction of the second levy component, which has no cap for individual institutions. As this levy component increases proportionally with assets, the entities with the most assets will contribute a substantial proportion. A corresponding benefit accrues to small and medium-sized entities.

14. In summary, the main points that will be of interest to levied institutions are as follows.

15. The total levy funding requirement for 2005-06 is forecast at $103 million, an increase of $6.5 million or 6.7 per cent compared with 2004-05.

16. The first, restricted component of the levies (based on direct cost of supervision) is estimated to raise some 73 per cent of APRA's levy funding requirement plus the requirements for the Australian Securities and Investments Commission (ASIC) and Australian Taxation Office (ATO). The second, unrestricted component (with a system impact and vertical equity rationale) is estimated to raise some 27 per cent of APRA's levy funding requirement.

- The restricted levy component in each sector has been calculated as reflecting the costs incurred by APRA in relation to direct supervision of entities in the sector. The unrestricted levy component figures are calculated based on indirect costs associated with analysis of risk by industry rather than by institution.

17. The general insurance sector will contribute a greater proportion of the levies than in 2004-05, with all of the other sectors contributing slightly smaller proportions. This reflects the increased focus and resources dedicated to this sector over the past years.

18. The smallest entities in the general insurance, life insurance and authorised deposit-taking institution (ADI) sectors will pay similar levy amounts in 2005-06 to what these paid in 2004-05. In particular, adding the unrestricted levy component for these smallest entities to the minimum amount for the restricted levy component gives a total approximately equal to the 2004-05 minimum levy amount in each sector.

19. In the superannuation sector, small APRA funds (SAFs) have been separated from other superannuation funds. The minimum amount for SAFs has been reduced**.**

20. The percentage levy rate (ie the sum of rates for the two components) in 2005-06 has fallen substantially in all industry sectors compared with 2004-05. For ADIs, life insurance and superannuation, the reductions will be about 40 to 65 per cent. For general insurance, the reduction is closer to 20 per cent. (These percentage rate reductions are possible because of the increases in the maximum amounts for the restricted levy components and the unconstrained nature of the unrestricted levy components.) This benefits in particular the large number of medium-sized institutions.

21. The maximum levy amounts for the restricted levy component have been adjusted upward to reflect the current cost estimates (higher costs of supervising the largest entities than previously estimated). This, when combined with the new, unrestricted levy component, means that the largest entities in 2005-06 will pay more than double in levies the amount paid in 2004-05.

- Whereas institutions paying the maximum amount faced a zero marginal cost under the previous system, the new levy component means that they face a small, positive marginal cost for additional assets. However, the larger institutions will continue to benefit from lower overall effective levy rates than those faced by smaller institutions.

22. Non-operating holding companies (NOHCs) in the insurance sector will be subject to the same levy arrangements as ADI NOHCs.

## SUMMARY OF LEVY FUNDING REQUIREMENTS FOR 2005-06

23. The base for all levy calculations is the estimated funding to be provided to APRA, ASIC and the ATO to undertake the functions recovered by the financial sector levies. Table 1 summarises these estimated expenditure and funding needs for 2005-06.

24. The current budgeted total cost for APRA for 2005-06 is $93.4 million[1], with $14 million of APRA's costs being met through offsets. These offsets include fees expected from superannuation trustee licensing, direct funding from the Government for work arising from the HIH Royal Commission, fees generated from elective work requested of APRA (including that related to the implementation of the new Basel Capital Accord), cost recoveries from the provision of statistical data and interest earned on investments. In addition, APRA's reserves are forecast to increase by $3.5 million in 2005-06.[2] Taken together, this represents an increase of $5.4 million in net levy funding for APRA over what was budgeted for 2004-05.

25. In addition to APRA's requirements, the levies fund certain market integrity and consumer protection functions undertaken by ASIC and the ATO. For 2005-06, the current forecast is that the amounts relating to ASIC and the ATO will be higher than for 2004-05 by a total of $1.1 million. This is due to a Government decision to increase funding for the Superannuation Complaints Tribunal by $1.6 million (relating to the implementation of superannuation choice and the ongoing Government commitment to national consumer financial literacy) and a reduction in ASIC funding of $0.5 million.

26. Table 1 shows that the total levy funding requirement as currently estimated increases by $6.5 million (6.7 per cent) in 2005-06.

**Table 1: Operating costs and levy funding requirement ($ million)**

| **Levy determinants** | **2003-04** *actual* | **2004-05** *budget* | **2005-06** *budget* |
|---|---|---|---|
| APRA – expenses | 74.2 | 85.7 | 93.4 |
| Less: net cost offsets | 7.0 | 6.5 | 14.0 |
| Add: increase in reserves | 2.0 | (1.7) | 3.5 |
| **Net funding required for APRA** | **69.2** | **77.5** | **82.9** |
| **Levy funding required** | | | |
| i. APRA | 69.2 | 77.5 | 82.9 |
| ii. ASIC | 14.4 | 15.2 | 16.3 |
| iii. ATO | 2.4 | 3.8 | 3.8 |
| **iv. Total** | **86.0** | **96.5** | **103.0** |

1 Portfolio Budget Statement 2004-05, Treasury Portfolio (Budget Related Paper No1.16) p. 145, adjusted for the Superannuation Licensing of Trustees programme.

2 Portfolio Budget Statement 2004-05, Treasury Portfolio (Budget Related Paper No1.16) p. 146. The increase in reserves offsets the anticipated loss in 2004-05.

## THE TWO LEVY COMPONENTS AND FUNDING REQUIREMENT BY INDUSTRY SECTOR

31. As noted earlier, a fundamental feature of the new financial sector levy-setting framework that has a major impact on the levies collected from regulated entities is that the levies now consist of two components.

32. With some minor alterations (outlined below), the existing sectoral basis for imposing the financial sector levies will be retained in the new framework. That is, the new framework will still allocate the total levy funding requirement among each of the regulated sectors in proportion to the regulation aimed at those sectors.

33. In determining the levies under the new framework, the adopted methodology first allocates APRA's funding requirement into its direct and indirect costs of supervision. It then allocates these elements to the industry sectors in proportion to APRA's resources devoted to those sectors. The funding required for ASIC and the ATO is added to the direct APRA costs for each sector and the total used to derive the proposed restricted levy components for each sector. The unrestricted levy components are derived from the indirect APRA costs attributed to each sector. The unrestricted levy component figures are taken to reflect appropriately system impact and vertical equity considerations.

34. In response to the Review of Financial Sector Levies, APRA has undertaken more detailed costing based upon the activity reporting that has accumulated over a number of years. This has provided more rigorous analysis of both activity by industry sector and the nature of the activities being undertaken.

### TWO LEVY COMPONENTS

35. The first, restricted levy component continues from the old levy framework and relates to the cost of supervision. Under this component a single levy rate is imposed on assets subject to a maximum and minimum levy amount.

36. This levy component has been calculated for this paper as reflecting the direct costs incurred by APRA in supervising entities in the sector. The funding required by this component is recovered from each regulated industry sector in proportion to APRA's direct regulatory costs for that sector (as adjusted to take account of the ASIC and ATO elements), consistent with the principle that this component should be related to costs of supervision.

37. The second, unrestricted levy component is new and relates to potential system impact and vertical equity considerations. This levy component will be imposed on assets, without any maximum or minimum levy amount for individual institutions.

38. That is, this component will apply to all institutions (regardless of size) with the amount determined as the rate multiplied by the assets.

39. The funding required to be raised by this new component has been calculated based on APRA's activities that are industry-wide rather than specific to an institution.

40. This will reflect more closely the two primary cost drivers within APRA (specific supervision by entity and the whole of industry work carried out by risk specialists and

support staff) and achieve greater vertical equity within industry sectors by reducing the burden on middle-sized entities.

41. To reduce volatility, analysis of the allocation of work to direct supervision and industry is undertaken using data averaged from a four-year period. The four-year average is based on recorded activity for the previous two years, the forecast outcome for the current year and the estimate for the coming year. For 2005-06, the average will be calculated from the actual proportions in 2002-03 and 2003-04, the forecast for 2004-05 and an estimate for 2005-06.

42. The result of this analysis is that the direct component constitutes 73 per cent of APRA's costs and the indirect component 27 per cent. This is consistent with the Government's acceptance of the review's recommendation concerning the share of APRA's levy funding requirements that should be met from the portion of the total levy based in system impact and vertical equity considerations.

## ALLOCATION OF THE TWO COMPONENTS TO INDUSTRY SECTORS

43. The new framework retains the existing sectors with some minor changes, which generally have little impact on the levy determination outcome. The changes are as follows:

- retirement saving account assets are being incorporated into the ADI sector or life insurance sector according to the sector classification of the RSA provider;
- SAFs are being separated from other regulated superannuation funds (effectively becoming a sub-sector of superannuation), with SAFs levied at lower minimum rates. Such rates will reflect primarily the cost of registration; and
- authorised non-operating holding companies that are outside the ADI sector are being subjected to the financial sector levies and charged a flat fee in the same way as ADI NOHCs.

44. Both of the levy components are then allocated to each industry sector, reflecting the share of APRA's total supervisory effort devoted to each sector. Table 2 provides a year-by-year analysis of the proportion of time spent by APRA in supervising each industry sector for each levy component.

45. Table 2 also calculates the four-year averages of APRA's costs that will be used in deriving the 2005-06 levy allocations for each sector.

**Table 2: APRA's supervision by industry sector (%)**

| Industry sector | 2002-03 *actual* | 2003-04 *actual* | 2004-05 *forecast* | 2005-06 *estimate* | 2005-06 ***4 yr average*** |
|---|---|---|---|---|---|
| **1st component - cost of supervision** | | | | | |
| ADIs | 33.9 | 33.4 | 35.8 | 36 | **34.7** |
| Superannuation | 40.3 | 38.5 | 35.3 | 35 | **37.3** |
| Life insurance/Friendly societies | 8.9 | 8.9 | 9.9 | 10 | **9.4** |
| General insurance | 17.0 | 19.3 | 19.0 | 19 | **18.6** |
| **Total** | **100** | **100** | **100** | **100** | **100** |
| **2nd component – potential system impact/vertical equity** | | | | | |
| ADIs | 38.4 | 31.3 | 32.3 | 32 | **32.9** |
| Superannuation | 32.9 | 35.2 | 31.9 | 32 | **32.9** |
| Life insurance/Friendly societies | 11.2 | 8.3 | 8.9 | 9 | **9.6** |
| General insurance | 17.9 | 25.1 | 26.9 | 27 | **24.5** |
| **Total** | **100** | **100** | **100** | **100** | **100** |

46. Table 3 uses the four-year average data from the two levy components in Table 2 to calculate the overall supervisory time contributed by each industry sector for 2005-06. It compares this to proportions used to set levies in previous years.[3].

**Table 3: Percentage of time charged to supervising industry sectors, averages (%)**

| Industry sector | 2001-02 | 2002-03 | 2003-04 | 2004-05 | 2005-06 *estimate* |
|---|---|---|---|---|---|
| ADIs | 39.2 | 35.4 | 35.7 | 34.8 | **34.4** |
| Superannuation | 35.4 | 39.5 | 37.1 | 36.8 | **36.3** |
| Life insurance/Friendly societies | 12.5 | 11.2 | 11.4 | 11.2 | **9.5** |
| General insurance | 12.8 | 13.8 | 15.7 | 17.1 | **19.8** |
| **Total** | **100** | **100** | **100** | **100** | **100** |

47. The change in time-averaged activity for each of the industry sectors reflects the smoothed trend line with earlier years no longer being included. For example, ADIs decline as the higher proportion of activity in 2001-02 is no longer affecting the average.

[3] Prior years were based on a single levy component and used three and five year averaging.

On the other hand, general insurance reflects the sustained additional activity and reform being deployed in more recent years.

48. For superannuation, the 2005-06 four-year average also decreases slightly, again following a recent trend. This reduction can also be partly attributed to APRA's supervisory activity in 2001-02 no longer being included in the average calculations. In that year APRA devoted an unusually high proportion of its resources to superannuation.

49. For life insurance, the 2005-06 four-year average is lower than that calculated for the 2004-05 levies. Similar to ADIs, life insurers are being allocated a lower proportion of APRA's resources than early in APRA's existence.

50. In respect of general insurance, the proportion of APRA's supervision has risen in 2005-06 mainly due to a continuing high level of system-wide activity as new reform measures continue to be implemented.

51. The average percentage of time spent supervising sectors for each levy component is then used to apportion APRA's estimated costs to each sector. Table 4 illustrates the 2005-06 levy funding required for both levy components from each sector and compares this with the actual levy funding required from each sector for 2004-05.

**Table 4: Estimated cost per sector for APRA levy funding ($ million)**

| **Industry Sector** | **2004-05** | **2005-06 Restricted component** | **2005-06 Unrestricted component** | **2005-06 Total** |
|---|---|---|---|---|
| ADIs (including RSAs) | 26.9 | 21.1 | 7.3 | **28.4** |
| Superannuation | 28.5 | 22.7 | 7.3 | **30.0** |
| Life insurance/Friendly societies | 8.7 | 5.7 | 2.1 | **7.8** |
| General insurance | 13.3 | 11.3 | 5.4 | **16.7** |
| Total | 77.5 | 60.8 | 22.1 | **82.9** |

52. The funding requirements of relevant activities undertaken by ASIC and the ATO are added to APRA's funding costs to give the total levy requirements on each industry sector. This is shown in Table 5.

53. The new levy framework has no impact on how the relevant ASIC and ATO costs are apportioned among industry sectors: they are simply added to APRA's supervision cost relating to each sector.

54. The levy amount to be raised from each industry sector in 2005-06 is compared with the amounts raised in 2004-05. For 2005-06 an additional net amount of $1.1 million was added to ASIC's requirements to administer the Government decision to implement superannuation choice and its ongoing commitment to national consumer financial literacy, less a modest reduction for other ongoing ASIC activity.

**Table 5: Total levy required by industry sector ($million)**

| Industry sector | APRA net funding | ASIC costs | ATO costs | Total 2005-06 levy | Total 2004-05 levy |
|---|---|---|---|---|---|
| ADIs (incl. RSAs) | 28.4 | 2.6 | - | **31.0** | 29.5 |
| Superannuation | 30.0 | 10.0 | 3.8 | **43.8** | 41.6 |
| Life insurance/ Friendly societies | 7.8 | 2.0 | - | **9.8** | 10.7 |
| General insurance | 16.7 | 1.7 | - | **18.4** | 15.0 |
| *Total* | **82.9** | **16.3** | **3.8** | **103.0** | **96.9** |

## INDUSTRY STRUCTURE

55. For this discussion paper, it has been assumed that industry structure is substantially the same as that used to calculate the 2004-05 levies. Therefore, there should be little impact on the calculation of levies from changes in industry structure or size.
In calculating the final levies payable in 2005-06, further changes in industry structure and size will be taken into account as updated data are collected. Table 6 shows the number and asset value of institutions that will be used in the modelling of the 2005-06 levies in this paper.

**Table 6: Number of institutions and assets used in modelling the 2005-06 levies**[4]

| **Industry sector** | | **Number of institutions** | **Total asset base ($m)** |
|---|---|---|---|
| ADIs | – banks | 52 | 1,200,990 |
| | – building societies | 14 | 14,094 |
| | – credit unions | 182 | 34,945 |
| | - *Sub-total* | *248* | *1,250,029* |
| Super funds | – excluding SAFs | 1,978 | 367,303 |
| | – SAFs only | 7,040 | 2,718 |
| | - *Sub-total* | *9,378* | *370,021* |
| Life insurers | – Life insurers | 39 | 189,436 |
| | – Friendly societies | 31 | 5,434 |
| | - *Sub-total* | *70* | *194,870* |
| General insurers | | 140 | 77,920 |
| **Total** | | **9,476** | **1,894,061** |

4 The asset values used are as at 31 Dec 2003 but have been adjusted for asset growth over 2004.

## MAXIMUM AND MINIMUM LEVY AMOUNTS

56. The maximum and minimum amounts applying to the first, restricted levy component are important factors in determining the levies that institutions pay.

57. The new framework increases the statutory maximum for the restricted levy component to $1.5 million for all sectors for 2005-06. As has always been the case, the maximum levy set for each sector can be well below the statutory maximum.

58. With improved data from activity reporting over a number of years, additional analysis has been performed on the costs to APRA of supervising the largest institutions. The analysis shows that the costs of directly supervising the largest entities (ie excluding the industry-wide supervision activities) are higher than the previously determined maximum levy amounts. This reflects the complexity of the large institutions and the amount of work required to supervise them. Therefore the scenario presented in this paper adjusts the maximum levy amounts upwards in each of the sectors.

59. For ADIs, it is suggested that the maximum for the restricted component be raised to $1.4 million, slightly below the statutory upper limit of $1.5 million. For the insurance sectors, the proposed increases in the maximums are from $460,000 for life insurance and $470,000 for general insurance to $700,000. For superannuation, the maximum is increased from $100,000 to $200,000.

60. The Government's response to the review noted that the smallest institutions should not pay higher amounts as a result of changes in the framework arising from the review's recommendations. The levy amounts suggested in this paper meet that requirement.

61. The review recommended that SAFs be separate from other superannuation funds and that they be levied at lower minimum rates. The previous minimum levy for superannuation had been set in an attempt to strike a balance between the supervisory costs of SAFs and those of other small superannuation funds. Separating the two types of superannuation funds allows different minimum amounts to be set that more accurately reflect the costs of each type of fund.

62. In respect of SAFs, supervision is largely through registration and scrutiny of annual returns, with the focus of the process being the approved trustee. The suggested minimum rate for SAFs is to be $500, which is lower than the 2004-05 minimum rate for the superannuation sector of $600.

63. Supervision of other (non-SAF) superannuation funds is more intensive than for SAFs. Reflecting this, the suggested minimum levy for other superannuation funds should be higher, but not more than is being charged for 2004-05.

## POSSIBLE LEVY SCENARIO

64. This section illustrates a possible levy scenario, based on the new levy calculation framework and the data outlined in the preceding sections of the paper, to demonstrate the levy parameters that can result from the changes. The major parameters of the scenario are in Table 7.

**Table 7: Levy parameters from the new framework**

| Industry sector | Current Framework | | | New Framework | | | |
|---|---|---|---|---|---|---|---|
| | Min | Max | Rate | Min | Max | Rate 1* | Rate 2** |
| | $ | $'000 | % | $ | $'000 | % | % |
| ADIs – Local | 500 | 1,182 | 0.011 | 470 | 1,400 | 0.00602 | 0.000586 |
| ADIs - Foreign | 500 | 591 | 0.0055 | 470 | 750 | 0.00301 | 0.000586 |
| Superannuation (non-SAFs) | 600 | 99 | 0.042 | 570 | 200 | 0.01548 | 0.001986 |
| Life insurers/ Friendly socs. | 500 | 460 | 0.022 | 470 | 700 | 0.00739 | 0.001095 |
| General insurers | 5,000 | 470 | 0.034 | 4,000 | 700 | 0.02088 | 0.006975 |

* Rate 1 applies to the first, restricted levy component relating to cost of supervision
** Rate 2 applies to the second, unrestricted levy component relating to potential system impact and vertical equity considerations.

65. The following assumptions have been used in Table 7.

- The levy charges relating to the first, restricted component for foreign bank branches and specialist credit card institutions will continue to be calculated at half the rates (except for minimum levy amounts, which will be the same) applying to conventional ADIs. However the rates relating to the second, unrestricted component will be the same as the rate relating to a conventional ADI, on the basis that the potential system impact and vertical equity considerations are not diluted because of the sharing of the supervision burden by the overseas regulator.

66. In addition to the information shown in Table 7, it is intended that all NOHCs, including those in the general insurance sector, will be levied at a flat rate and that the minimum levy amount for SAFs is to be $500, as opposed to the $600 applying to non-SAF superannuation funds.

## IMPACTS ON INDIVIDUAL INSTITUTIONS

67. The next series of tables shows the levy amounts that would payable by various-sized institutions in each industry sector in 2005-06 using the levy parameters in Table 7 and compares this with the amounts paid in 2004-05 under the previous determination framework. The asset values chosen reflect the range of institution sizes within each sector.

**Table 8: Levy amounts on ADIs ($)**

| Asset Base | **$5m** | **$50m** | **$500m** | **$5b** | **$25b** | **$180b** |
|---|---|---|---|---|---|---|
| Previous | 550 | 5,500 | 55,000 | 550,000 | 1,182,000 | 1,182,000 |
| New | 499 | 3,302 | 33,015 | 330,153 | 1,546,622 | 2,455,680 |

**Table 9: Levy amounts on foreign ADI branches ($)**

| Asset Base | **$5m** | **$50m** | **$500m** | **$5b** | **$15b** |
|---|---|---|---|---|---|
| Previous | 500 | 2,750 | 27,500 | 275,000 | 571,000 |
| New | 499 | 1,797 | 17,974 | 179,739 | 539,216 |

**Table 10: Levy amounts on superannuation funds (excluding SAFs) ($)**

| Asset Base | **$1m** | **$3m** | **$50m** | **$250m** | **$5b** | **$20b** |
|---|---|---|---|---|---|---|
| Previous | 600 | 1,260 | 21,000 | 99,000 | 99,000 | 99,000 |
| New | 590 | 630 | 8,733 | 43,664 | 299,282 | 597,128 |

**Table 11: Levy amounts on life insurers/friendly societies ($)**

| Asset Base | **$5m** | **$50m** | **$500m** | **$3b** | **$10b** | **$50b** |
|---|---|---|---|---|---|---|
| Previous | 1,100 | 11,000 | 110,000 | 460,000 | 460,000 | 460,000 |
| New | 525 | 4,242 | 42,418 | 254,507 | 809,464 | 1,247,318 |

**Table 12: Levy amounts on general insurers ($)**

| Asset Base | **$5m** | **$25m** | **$250m** | **$750m** | **$3b** | **$9b** |
|---|---|---|---|---|---|---|
| Previous | 5,000 | 8,000 | 80,000 | 24,000 | 470,000 | 470,000 |
| New | 4,349 | 6,964 | 69,640 | 208,919 | 835,694 | 1,327,748 |

68. These tables show the overall impact of the new levies determination methodology under this scenario as follows.

69. The smallest entities generally pay about the same as in 2004-05 (the reasons for which have been explained in the ‘maximum and minimum amounts’ section).

70. There is a wide range of asset values where entities pay lower levy amounts. This reflects the lower levy rates under the new framework compared with the previous one.

71. The largest entities in each sector will pay more than in 2004-05. This is due to both the higher maximum restricted levy amounts and the new, unrestricted levy component. In the previous framework, once the maximum amount was reached, all large entities paid the same levy. The tables show that, under the new framework, levies continue to increase with assets because of the new levy component. This means that entities with significantly different asset levels, but both above the threshold for the maximum levy amount (or maximum restricted levy component amount), will no longer pay the same levy amount.

72. Table 13 shows the impact of the lower levy rates and higher maximum amounts on the value of assets that would be held by an institution at the minimum and maximum levy amount thresholds of the first, restricted levy component. The asset thresholds for both minimums and maximums have increased. Therefore a greater number of institutions

will pay the minimum amount and a smaller number of institutions will pay the maximum amount.

**Table 13: Asset thresholds for reaching minimum and maximum amounts on the restricted levy component**

| **Sector** | **Minimum ($m)** | | **Maximum ($b)** | |
|---|---|---|---|---|
| | Previous | New | Previous | New |
| ADI local | 4.5 | 7.8 | 10.7 | 23.3 |
| ADI foreign | 9.1 | 15.6 | 10.7 | 23.3 |
| Superannuation (non-SAF) | 1.4 | 3.7 | 0.2 | 1.3 |
| Life insurance/ Friendly societies | 2.3 | 6.4 | 2.1 | 9.5 |
| General insurance | 15.6 | 19.2 | 1.5 | 3.4 |

## POSSIBLE TRANSITIONAL ARRANGEMENTS

73. The recommendations of the Review of Financial Sector Levies that were accepted by the Government included one relating to transitional arrangements. In particular, Recommendation 15 was that, for the first two years of the new arrangements, the determination of the levies take into account the magnitude of changes in the actual levies from the previous year. Where application of the principles recommended by the review might lead to particularly substantial changes in the levies from those of the previous year, that application should be able to be modified to reduce the extent of change in a particular year. The intention behind this recommendation was to ensure that the new arrangements would not cause undue financial hardship for levy-paying entities.

74. The magnitude of the changes in the levies that would result from the full adoption of the new arrangements, while significant, seems unlikely to cause financial hardship for levy-paying entities. The levies should remain a very small proportion of any individual institution’s assets. Therefore, the transitional arrangements in relation to the 2005-06 (or 2006-07) levies do not appear necessary. Accordingly, it is proposed that the new levy determination framework apply fully in these years and that transitional arrangements not be applied.

75. Industry comments in relation to this proposal would be welcome.

# ATTACHMENT A: GOVERNMENT RESPONSE TO THE REPORT OF THE REVIEW OF FINANCIAL SECTOR LEVIES

The Government has agreed that:

(1) The sectoral basis for imposing the financial sector levies be retained.

(2) Subject to Recommendations 3, 4 and 5, the existing sectoral distinctions be retained.

(3) The levies imposed on retirement savings account (RSA) providers be merged with the levies imposed on the authorised deposit-taking institution (ADI) and life insurance sectors according to the sector of the RSA provider, but that the Retirement Savings Account Supervisory Levies Imposition Act 1998 not be repealed.

(4) Authorised non-operating holding companies that are outside the ADI sector be subject to the financial sector levies.

(5) The levy arrangements for small APRA superannuation funds (SAFs) be separated from those for other superannuation funds and, in particular, that SAFs be levied at lower minimum rates than other superannuation funds.

(6) Changes to the levy determination arrangements will not lead to increases in the amounts paid by the smallest financial institutions.

> In part, this reflects the Government's acceptance of the review's conclusion that system risk and vertical equity considerations, as well as cost, should be taken into account in the determination of levies. In addition, the Government considers that small financial institutions fill an important niche in terms of alternate service provision, competition and choice for consumers.

(7) There be two distinct elements to the financial sector levies.

> One component to relate to the cost of supervision and involve a single levy rate on assets subject to a maximum (as well as a minimum) levy amount along the lines of the existing levy arrangements; and
>
> the other component to relate to potential system impact and vertical equity considerations and be a low-rate levy on assets, without any maximum levy amount.

(8) The portion of the total levy based in system impact and vertical equity considerations be set such that it is raises between 10 and 30 per cent of APRA's levy funding requirement in any one year.

(9) A statutory upper limit on the maximum levy amount payable by any regulated institution in each sector apply only to the cost-based component of the recommended new levy structure.

(10) The statutory upper limit for the cost-based component of the levy on an entity for all financial industry sectors be $1.5 million in 2005-06 and be increased by an indexation factor for each subsequent year.

(11) The indexation factor applied to the statutory upper limits for each year be based on the movements in the Consumer Price Index specified under existing arrangements PLUS three percentage points.

(12) Total assets remain the base for the financial sector levies.

(13) Sectoral levy rates continue to be revisited – and, if appropriate, adjusted – each year.

(14) Levies for each industry sector be determined on the basis of a four-year moving average of estimated expenditure for that sector.

(15) For the first two years of the new arrangements, the determination of the levies take into account the magnitude of changes in the actual levies from the previous year. Where changes in the levies from the application of the principles recommended by the review might be particularly substantial, that application should be able to be modified to reduce the extent of change in a particular year.

(16) The activities for which financial sector levy funds are raised be continued and that APRA, ASIC and the ATO ensure that their reporting of the use of the levy funds satisfies the requirements of the Government's cost recovery policy.

(17) The next review of the levy-setting arrangements take place during 2008.