

Australian Government Guarantee Scheme for Deposits and Wholesale Funding

Steven Goodman, Truman Hoyle Lawyers

1. Background

In response to considerable turbulence in international financial markets and other governments introducing similar schemes the Australian Commonwealth Government (“Government”) introduced a scheme on 12 October 2008 to guarantee certain deposits and wholesale funding of eligible authorised deposit taking institutions (“ADI”).

ADI’s include Australian owned banks, Australian incorporated subsidiaries of foreign banks, branches of foreign banks (with some restrictions), building societies, credit unions and other ADI’s. A complete list of ADI’s or Eligible Institutions is available in Schedule 1 of the Scheme Rules at www.guaranteescheme.gov.au.

The rationale for covering only ADI’s is that they are subject to prudential regulation by the Australian Prudential Regulation Authority (see www.apra.gov.au) in accordance with international standards.

The aim of the scheme is to promote financial system stability in Australia by supporting confidence and assisting ADI’s to continue to access funding and to ensure that Australian institutions are not at a disadvantage compared to international competitors that can access similar schemes in other countries.

The scheme was changed on 28 November 2008 and there is now a clear distinction between:

- ADI deposits of up to AUD\$1million per customer per institution which are guaranteed automatically for free by the Government; and
- ADI deposits over AUD\$1 million and certain wholesale funding liabilities which are only guaranteed following approval of an application made by an institution for a particular account or product and payment of a prescribed monthly fee.

Prior to the scheme being introduced there was no general government guarantee for deposits or any other products issued by financial institutions. There was however a provision in the Banking Act 1956 (Section 13A), which still exists, which provided for priority for ADI deposit liabilities in the event an ADI becomes unable to meet its obligations.

2. ADI Deposits up to AUD\$1 Million

These are guaranteed automatically for free by the Government under the Financial System Legislation Amendment (Financial Claims Scheme and other Measures) Act 2008, Banking Act 1959 – Declaration of Covered Financial Products and Banking Amendment Regulation 2008 (No.1) (Copies are available through www.treasury.gov.au).

The threshold of AUD\$1 Million applies per depositor per institution. Therefore separate deposit accounts held by a depositor at an institution will be aggregated for the purpose of the threshold. Accounts held at separate institutions will not be aggregated for the purpose of the threshold.

A complete list of the types of covered accounts is set out in a declaration made by the Government which is available at www.treasury.gov.au.

The deposit guarantee does not apply to products that are not deposit products with ADI's. Market linked investments products such as share portfolios and managed funds including mortgage trusts, property trusts and debentures are not covered. In addition, retirement income products including annuities are also not covered.

The deposit guarantee applies to deposits held in ADI's regardless of the identity or location of the depositor. It also applies to deposits held in any currency.

Deposits held by ADI foreign (non Australian) bank branches located in Australia are not covered automatically. They can access the guarantee by applying and paying a fee (as specified in 3 below) but only in respect of domestic deposits held by Australian residents at call or with maturities up to and including 31 December 2009 subject also to further conditions.

3. ADI Deposits over AUD\$1 Million

These are only guaranteed by the Government following approval of an application made by an ADI to the Reserve Bank of Australia. This part of the scheme and the Wholesale Funding Liabilities component referred to below was implemented via a Deed of Guarantee and Scheme Rules issued by the Government and available at www.guaranteescheme.gov.au.

The process for making applications is set out in the Scheme Rules.

Once an application is approved the Government issues an Eligibility Certificate which certifies that specific liabilities set out in the certificate are guaranteed. Copies of these certificates are placed on the website at www.guaranteescheme.gov.au.

The fees that are payable by institutions for the guarantee depend on the long term credit rating of the ADI. They are 0.7% per annum for AAA to AA-, 1% for A+ to A- and 1.5% for BB+ and below. Most institutions are passing these fees on to their customers.

4. Wholesale Funding Liabilities

The process for making applications, issue of Eligibility Certificates and fees are in essence the same as for the guarantee for ADI deposits over AUD\$1 million. However, not all wholesale funding liabilities of ADI's are eligible for the guarantee.

Short term wholesale funding liabilities are eligible to be covered if they are senior unsecured debt instruments with maturities up to 15 months which are "not complex" and they are bank bills, certificates of deposit, transferable deposits, debentures or commercial paper. For ADI foreign (non Australian) bank branches only maturities of up to 31 December 2009 are covered subject also to further conditions.

Term funding liabilities of between 15 to 60 months are also eligible to be covered but the instrument must be a bond, note or debenture and it must also be "non complex".

In addition applications can also be made for issuance programs to be covered.

Term wholesale funding liabilities of ADI foreign (non Australian) bank branches are not covered.

The Government has issued guidelines on the interpretation of “non complex”. These can be found at www.guaranteescheme.gov.au. The issue of an Eligibility Certificate is conclusive evidence that the liability the subject of the certificate has been accepted by the Government as “not complex”.

5. Timing

The Government has stated that the deposit guarantee will be in place for a period of 3 years (until October 2011) and that the wholesale funding guarantee will be available until market conditions have normalized.

The scheme rules may be changed at any time by the Government.

6. Conclusions

Account holders of ADI deposits over AUD\$1 million (per institution) or holders of wholesale funding liability products issued by ADI's that want to ensure that a specific account or product is backed by the Government guarantee should obtain and check the Eligibility Certificate for that account or product.

There is no doubt that the scheme has assisted ADI's to continue to access funding in the current turbulent financial markets. However, the scheme has caused a considerable shift of funds away from non covered products such as managed funds towards ADI's, in particular the four major Australian banks. The impact of this shift of funds is working against the aim of promoting financial system stability.

7. Further Information

Further information is available at www.treasury.gov.au and at www.guaranteescheme.gov.au.

Steven Goodman
Partner
sgoodman@trumanhoyle.com.au
Truman Hoyle Lawyers
Tel: (02) 9226 9888
Fax: (02) 9226 9899

Truman Hoyle is a Sydney based law firm specialising in six complex and dynamic areas of law, being corporate law, communications law and regulation, technology law, media and e-commerce law, energy law and regulation and industrial law. Australasian Legal Business has recently ranked the firm's Telecommunications Media & Technology and Intellectual Property practices as top-tier in Sydney. The firm was named Australian Law Firm of the Year in 2005 and again in 2006, for firms with 50 lawyers or less.

March 2009
© Truman Hoyle Lawyers 2009