

7 February 2025

Council of Financial Regulators and
Australian Competition and Consumer Commission



Via email: CFRReview@treasury.gov.au

Review into Small and Medium-sized Banks

About AFMA and its members

The Australian Financial Markets Association (AFMA) is the peak industry body for Australia's financial markets industry – including the capital, credit, derivatives, foreign exchange, and other specialist markets. AFMA represents more than 130 industry participants from Australian and international banks, leading brokers, securities companies, government treasury corporations to asset managers, energy firms, carbon market participants, and industry service providers.

AFMA promotes efficiency, integrity, and professionalism in Australia's financial markets enabling the markets to continue to support the Australian economy, high skilled job markets and the energy transition.

AFMA's policy approach

AFMA members are principally participants in wholesale capital markets and do not, by and large, provide services or products to retail customers. Therefore, AFMA, as an organisation, applies a wholesale lens to the appropriateness of policy and regulatory settings, which may not be wholly aligned with a retail perspective. We continue to highlight areas where a retail approach is not fit for purpose in a wholesale context, or issues in which the resulting impact on wholesale markets has not been duly considered.

AFMA understands the Review of Small and Medium-sized Banks (**the Review**) is focused on examining the state of the small and medium banking sector, with a focus on competition. Contained within this cohort of banks are foreign banks operating in Australia. These banks are the focus of AFMA's submission and, as discussed below, are critical to the ongoing prosperity of Australia and the ability of Australian businesses to access essential financial products and services.

In addition to focusing on foreign banks operating in Australia, AFMA's submission highlights challenges and opportunities regarding the evolution of Australia as a financial services centre. Some of the related issues are outside the remit of the Council of Financial Regulators (**CFR**) but highlight the need for governments and regulators at all levels to collaborate for the broader benefit of Australia's financial system.

Competition, growth, international alignment and the building deregulation agenda

Financial services are an important part of the Australian economy providing both direct and indirect benefits. Foreign banks operating in Australia are critical to the provision of those financial services, particularly as they relate to financial markets; services that are critical to businesses in Australia, both those operating domestically and those with international reach.

Despite the significant role of foreign banks in providing financial services, much of the national debate regarding banking in Australia concentrates on the role of the major banks versus domestic non-major banks. Viewing banking in Australia as a dichotomy of these two groups misses the important and

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significant role that the sector and foreign banks play in supporting the Australian economy and Australian businesses.

It also misses the global context in which banking, especially financial markets, operate. By often ignoring this context, we risk missing opportunities to achieve our national potential and to support the competitiveness of Australia's financial services industry in Australia and in the region. The focus of major versus non-major banks is also evident in the development of the finance industry's rules and requirements, where the broader system, foreign banks and our ability to compete in the region are at times given little or no consideration.

Notwithstanding this, generally, Australia's regulatory and legislative regimes provide for financial markets and foreign banks to operate competitively and effectively in Australia and to support Australian customers. However, more prominent consideration of the impacts of current requirements and proposed changes on financial markets, foreign banks and their customers would reduce unnecessary regulatory burdens, costs and inefficiencies. Ultimately, this would result in increased competition, provision of services and local employment.

The need to consider our global competitiveness has arguably increased with a growing shift towards deregulation and key peer jurisdictions further delaying the implementation of internationally agreed rules, such as the Basel III Post-Crisis Reforms. These rules, for example, were effective in Australian from the start of 2023 and are yet to be implemented in jurisdictions such as the European Union, United Kingdom and United States.

In fact, major global financial jurisdictions are going further than delaying new requirements. For example, a deregulation agenda has built significant momentum in the USA. While in the UK, the Financial Conduct Authority has publicly stated that "Growth will be a cornerstone of our strategy, through to 2030"¹, similar to changes by the Monetary Authority of Singapore (**MAS**). Further, the FCA identified "areas where further Government action could enhance our collective efforts", being:

- Unlocking capital investment and liquidity;
- Accelerating digital innovation to enhance productivity;
- Reducing the regulatory burden;
- Making it easier for firms to start up and grow;
- Improving exports and inward investment; and
- Certainty and predictability.

Other examples of supportive foreign regimes are discussed in the attached appendix.

Key findings and recommendations

The momentum of such global efforts means that, it will not be enough to maintain the status quo. If Australia wishes to remain competitive and wants to maintain its domestic financial services capabilities, that Australian businesses rely upon, it will need to respond in a supportive manner.

Given its role of oversight and management of the financial system, there is an opportunity for the CFR to be a driving force in creating a more supportive and efficient regime. Doing so would enhance the competitiveness and reputation of Australia as a financial services centre, and the ability of financial markets and foreign banks to support customers and the economy.

AFMA recommends that government agencies explicitly consider the impact of their existing requirements and any proposed changes on the attractiveness and competitiveness of Australia as a financial centre, and in particular, the ability of financial markets and foreign banks to support customers and the economy.

¹ Financial Conduct Authority (2025) [RE: A NEW APPROACH TO ENSURE REGULATORS AND REGULATIONS SUPPORT GROWTH](#), Letter to the UK Prime Minister, Chancellor, and Secretary of State, 16 January

Further detail on AFMA's position is contained in the attached appendix.

AFMA would welcome the opportunity to discuss this submission further and would be pleased to provide further information or clarity as required. Please contact Brendon Harper at brendonh@afma.com.au or 0411 281 562.

Regards,

A handwritten signature in black ink, appearing to be 'B. Harper', with a long, sweeping horizontal line extending to the right.

Brendon Harper
Head of Banks and Prudential

Appendix A

1. Role of financial markets and foreign banks in Australia

At their core, financial markets contribute to increased productivity and economic growth on a sustained basis through two primary means:

- providing high quality, innovative and cost-effective financial intermediation, risk management and investment services to Australian businesses, governments, and consumers; and
- enhancing the attractiveness of Australia as an international financial centre, by providing services to overseas clients, investment opportunities in Australia, and generating employment, income, and tax revenue in Australia.

Australia's financial markets are considered efficient, professional and to operate with integrity.² Both domestic and foreign banks contribute to the effective operation of Australia's financial markets. However, much of the national debate in Australia regarding banking concentrates on the role of the major banks versus non-major banks. Viewing banking in Australia as a dichotomy of these two groups misses the important and significant role that foreign banks play in supporting the Australian economy and Australian businesses.

In Australia, foreign banks largely offer wholesale and institutional services³ and are a significant part of the engine of the Australian economy and investor basis. Foreign banks play a unique role in the Australian economy in that they help bring investors into Australia and assist Australian companies and investors access foreign markets and important financial products. In this sense, foreign banks provide a complementary element to domestic banks in the provision of financial services in Australia. With their global networks and reach, foreign banks provide, among other benefits, greater access to additional (capital) markets and a wider range of risk management services, that are relied upon by Australians, Australian businesses and Australian governments, than would otherwise be available.

Currently, there are over 50 foreign banks operating in Australia⁴ providing a wide range of supportive products and services. Despite their largely wholesale focus foreign branches account for 9.5% of banking assets, as noted in the Review's issues paper (page 4). Considering all foreign banks, total banking assets held increases to over 13% – more than regional banks⁵ and Macquarie Bank combined, who collectively hold less than 10%, with all other non-major banks holding 6.5% of total assets (Graph 1).⁶ Additionally, foreign banks are particularly important in supporting Australian businesses' financing needs, providing 24% of lending to non-financial businesses (and 37% to financial institutions; Graph 2). By contrast, all other non-major banks, including regional banks and Macquarie Bank, provide approximately 7% of lending to non-financial businesses.

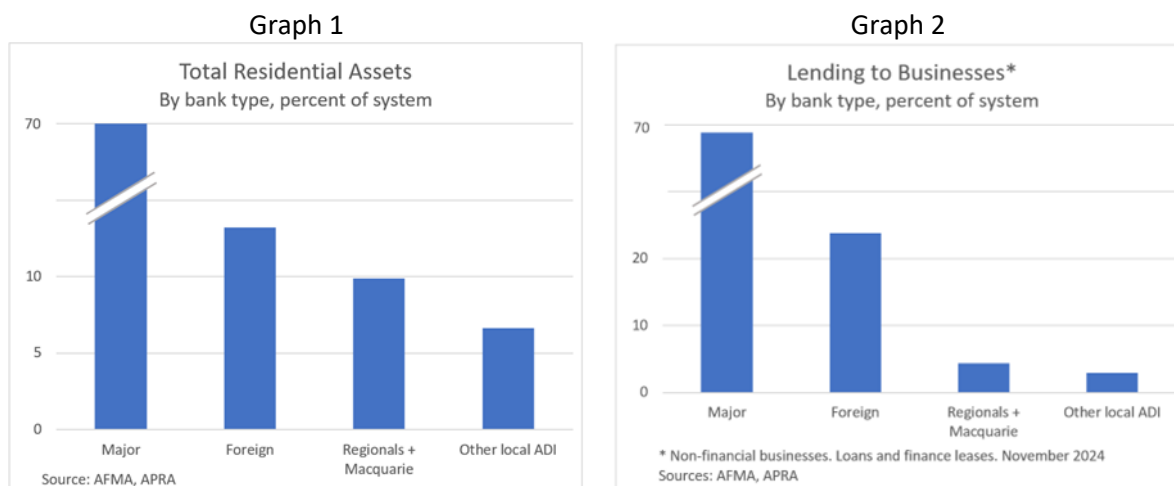
² For example, the Australian Investment and Securities Commission's (ASIC) report into equity markets concluded that "Australia's equity markets continue to operate with a high level of integrity and remain consistently among the cleanest in the world." ASIC (2024) [Australians can be confident in the integrity of our equity markets: ASIC report](#), Media Release, 24-182 MR, 24 July

³ A small number of foreign banks, who operate foreign subsidiaries in Australia, are also able to offer retail products.

⁴ Foreign subsidiaries and foreign branches, according to APRA's [Register of Authorised Deposit-taking Institutions](#).

⁵ AMP Bank, Bank of Queensland, and Bendigo & Adelaide Bank.

⁶ Australian Prudential Regulation Authority (APRA) Monthly Authorised Deposit-taking Institution Statistics, November 2024



In addition to lending, foreign banks are particularly important in supporting financial markets and assisting business manage risks and operate across borders. For example, foreign banks are instrumental in facilitating Australian businesses' risk transfer and mitigation, such as through swaps and derivatives in cross-currency, interest rate and inflation products. Foreign banks also support functioning debt capital markets by acting as intermediaries between issuers of debt and market investors. They provide specialised services across the bond issuance lifecycle, including structuring, timing, pricing, documentation drafting, execution and planning of debt offerings.

Australia's funding and financial markets could not operate as effectively and efficiently as they do without the active participation of foreign banks. As such, it is critical that as governments and government agencies actively consider the importance of foreign banks in the policy formulation process. Failure to consider foreign banks and their customers, or considering them as an afterthought, jeopardises the ability of Australian businesses to operate and the Australian economy to grow and flourish, as discussed in more detail below.

2. Australia as a financial centre

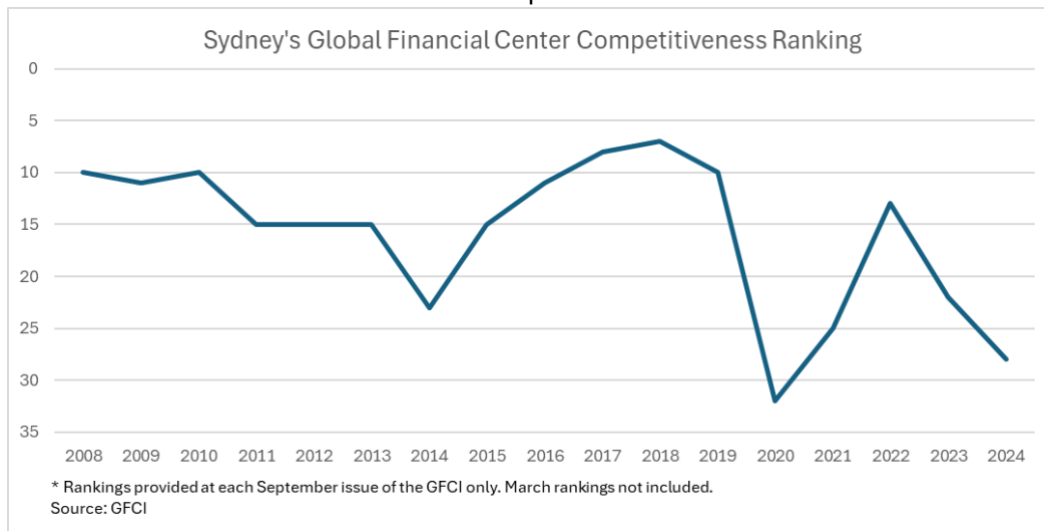
Australia has a goal to be a leading global and regional financial centre. The approaches and requirements of CFR agencies have a role to play in supporting this goal.

The benefits and merits of this goal is evidenced by the bipartisan support shown to the recommendations of the 2009 Johnson Report into Australia as a Financial Centre. However, notwithstanding stated support for Australia's financial centre capability at a Governmental level, objective evidence is that the relative attractiveness of Australia as a location to conduct financial centre activity has been in sharp decline.

An indicator of Australia's progress towards creating an environment to foster us becoming a leading global and regional financial centre is the Global Financial Centre Index (**GFCI**), which assesses and ranks the competitiveness of financial centres globally on a bi-annual basis. In the years leading up to 2019, Sydney consistently placed in the top 15 most competitive financial centres globally (Graph 3). However, since then, Sydney's performance has slipped, falling to 28th place in the most recent September 2024 ranking.⁷

⁷ [Global Financial Centres Index](#)

Graph 3



These results confirm two realities for the Australian economy and our industry more specifically:

1. Australia's financial centre competitiveness has not recovered from the pandemic. Markedly, rather than seizing the opportunity for economic growth through reinvigoration of the markets presented following the end of the pandemic (c. mid-2022), Australia's financial centre competitiveness has continued to decline, primarily due to positive steps being taken by other centres to enhance their attractiveness.
2. The perception of Australia as a place to conduct business dropped and has consistently remained lower since the Hayne Royal Commission. It is AFMA's assessment that in responding to the review and implementing its recommendations, adequate weight was not given as to the resulting impact on Australia as a place to do business and as a destination for capital. It has become harder and more costly to do business in Australia.

In contrast to Australia, other jurisdictions have prioritised increasing their attractiveness as global financial centres.

2.1. Comparative position with other global financial centres

While post-pandemic economic recovery is not a uniquely Australian problem, other advanced economies have sought to reinvigorate their financial markets through a calculated series of targeted initiatives to boost their financial centre competitiveness, driving business activity. Perhaps unsurprisingly, our greatest regional competitors outrank us as a place to do business. Singapore, Hong Kong, Seoul, and Shanghai are all in the world's top fifteen most competitive financial centres according to the GFCI.

Notable actions by governments offshore have bolstered their financial centre's dynamism and competition. Testimony from the Seoul Metropolitan Government, on Seoul's rise in the index explains "Seoul believes global financial companies are our true partners for growth. There are many incentives provided to global financial companies that enter Seoul..."⁸. AFMA also understand that the Korean Government opened the Seoul Financial Hub in 2021 to help foreign companies look to start or resume businesses in the city to evaluate domestic market conditions, obtain necessary licenses, find top local talent and handle tax and accounting issues.

While the Hong Kong Financial Services Development Council submitted: "As of March 2020, 110 of the 137 policy recommendations had been adopted by the Government and relevant regulators since

⁸ Financial Centre Future (2021) *The Global Financial Centres Index 30*, September, p.60

FSDC's inception in 2013."⁹ Likewise, in Singapore, the Government revised the MAS mandate to specifically include regard for boosting competitiveness. MAS likewise issues an annual financial services industry transformation map which sets out its vision areas for the year and strategic areas for growth.

Similar action was taken in Europe by the UK Government with new remit letters issued to both the Prudential Regulation Authority (**PRA**) and FCA with clear, targeted recommendations on growth and international competitiveness – the FCA's response being discussed above. The City of London Corporation likewise has a dedicated Minister who aids the growth of London's financial centre, and the City of London Corporation has an ongoing campaign that showcases and promotes the UK's offer for financial and professional services. All of these initiatives send a signal that the jurisdiction is open for financial centre business and that the Government and regulators will partner with businesses to enhance the opportunities for such businesses to flourish. The absence of similar commitments from the Australian Government likewise sends a signal, that Australia is not as committed to attracting and retaining mobile financial businesses to Australia.

3. Regulatory burden and proportionality

Considering more specifically the remit of CFR agencies, a key area for potential improvement in the competitiveness and efficiency of Australia's financial system is reducing regulatory burden through the increased application of proportionality, specifically substituted compliance.

In considering proportionality for foreign banks, it is important to understand how local requirements add to the already comprehensive and complex requirements already imposed upon these institutions. Foreign banks operating in Australia are, rightly, required to comply with Australian laws and regulations. They are also required to comply with the relevant laws and regulations of their home jurisdiction and any other jurisdictions in which they operate.

Considering prudential requirements, for example, a foreign bank with operations in Australia, the European Union, the United Kingdom, the United State and Singapore would need to consider and abide by prudential regulations from (among others) APRA, the European Banking Authority, the PRA, the Federal Reserve and the MAS. All of these jurisdictions are signatories to the Basel Committee on Banking Supervision (**BCBS**) with materially similar regimes. While AFMA is supportive of requirements tailored to national circumstances, in reality, this results in foreign banks needing to comply with a myriad of often materially similar but slightly different requirements with diminishing additional value or protection created by each new layer of regulation.

APRA's risk-based approach and delineation between 'Significant Financial Institutions' (**SFIs**) and non-SFIs is to be commended and has reduced the regulatory burden on non-SFIs by limiting the range of requirements they need to comply with. This has also helped APRA to free up and concentrate more of its resources and supervisory activities over entities that pose greater prudential risk to the Australian economy. However, similar to considering banking in Australia as a dichotomy of the major banks and non-major banks, this distinction does not sufficiently capture the unique circumstances, abilities and safeguards present in foreign banks.

As highlighted above, foreign banks are required to be compliant in various jurisdictions. As a result, they have well developed and tested global frameworks and resources across risk management and compliance, subject to supervision by BCBS and International Organization of Securities Commissions (**IOSCO**) aligned regulators. Duplicating these frameworks and resources in Australia can provide

⁹ *Ibid.*

minimal or no additional prudential safety or assurance while contributing to costs and reducing the attractiveness of Australia as a place to conduct business.

A way to reduce this duplicative burden is to increase the application of substituted compliance for foreign banks where they are subject to equivalent, or near equivalent, requirements in other jurisdictions. The benefits of this would be reduced costs in providing services to Australian customers with more options and an increase in competition in the banking sector, leading to the increase in the relative competitiveness of Australia as a financial centre.

4. Additional options to improve Australia's attractiveness

A supportive legal and regulatory environment is fundamental cornerstone of a competitive, dynamic and flourishing financial sector. Indeed, “[c]ompetition and economic dynamism should be considered complementary parts of the economic ecosystem.”¹⁰

While Australia has a reputation of having a relatively stable business environment, it arguably continues to fall behind comparable countries with regards to its competitiveness and dynamism. The House of Representatives Standing Committee on Economics, for example, concluded that “Australia needs to lift its game when it comes to both competition and economic dynamism... If we don't tackle this challenge, future generations will be left poorer. The potential upside is massive: higher growth rates, higher incomes and better outcomes for consumers.”¹¹

Government regulatory and legislative settings have a role to play in promoting competition and dynamism. It is imperative that government explore initiatives that safeguard our standing as a stable business environment and reinvigorate our dynamism, as other competing jurisdictions have successfully done.

Specifically, regarding the financial industry, AFMA sees a number of initiatives that would help with better policy design, implementation and regulatory approaches, some of which fall within the CFR's mandate.

- The establishment of an independent expert body that can provide advice and recommendations to relevant Ministers about matters relating to corporations and financial services law, administration, and practice. This could operate in similar effect to the previous Corporations and Markets Advisory Committee. Such a body would be well placed to appropriately consider relevant issues, differentiate where relevant between wholesale and retail, and oversee industry wide simplification and sophistication of financial services law and regulation. A properly constituted body of this type could act as a key conduit between business and Government;
- Financial Regulator Assessment Authority (**FRAA**) reviews of both APRA and ASIC as essential in ensuring effectiveness and capability. AFMA was disappointed in the 2023-24 Budget decision to reduce the FRAA review cycle from a biennial basis, as mandated as part of the Hayne Royal Commission, to a five yearly cycle. With the ever-growing regulatory priorities of regulators and changing nature of finance globally, we believe a five yearly review cycle is out of pace with the rate of change within the sector and poses both threats to consumers and the efficient function of industry. Such a cycle would also effectively dismantle the FRAA structure, as FRAA panellists would have little incentive to remain given the time between reviews – this has borne out in practice through the resignation of each FRAA panellist since the Government announcement AFMA supports the re-instatement of the biennial review cycle;

¹⁰ House of Representatives Standing Committee on Economics (2024) [Better Competition, Better Prices: Report on the inquiry into promoting economic dynamism, competition and business formation](#), March, p.iii

¹¹ *Ibid*, p.iv

- Reform of the Corporations Act 2001. AFMA strongly supported the work of the Australian Law Reform Commission (**ALRC**) and its subsequent recommendations. Over a year on from the ALRC's report to Government and we are yet to see a pathway for reform, including in the recently published regulatory initiatives grid. The current state of the Act makes business operations complex, costly, and challenging to operate within for both industry and regulators alike. AFMA supports the ALRC's recommendations to establish a body to carry forward the recommended reforms; and
- Many competing jurisdictions are OECD members, and respective regulators share Memorandums of Understanding. Therefore, locally we believe due deference should be given to offshore jurisdictions, particularly in relation to comparable licensing regimes in offshore jurisdictions. Divergences from globally recognised standards or duplication of reporting creates unnecessary regulatory burden and adds significant compliance costs. The [2021 Australia as a Financial & Technology Centre Advisory Group report](#) (page 60) highlights:

“A fund, or other financial business, that moves from Hong Kong, Singapore or London would, under current ASIC policies, need to apply for a standard AFS licence as a new entity or apply for a foreign AFS licence. In the Committee's view, it would be preferable to encourage suitable entities to obtain a full standard AFS licence and this is best done by making this process quick and easy for the right entities. The regulatory frameworks in these three markets are reasonably comparable to Australia and have a shared history and common law basis. While the precise rules diverge, the overall standard of supervision is considered to be comparable. This Recommendation would reduce the regulatory obligations and the compliance costs for businesses to receive a licence to be able to operate in Australia, especially where they may wish to relocate activities currently being conducted in Hong Kong, London or Singapore. In addition, it would promote organic business growth and employment, by providing more certainty and an expedited process for foreign businesses that are looking to expand their operations and activities to Australia.”

4.1. Tax and cost competitiveness

The competitiveness of a jurisdiction's taxation settings is a principal driver of where business is conducted and where capital is deployed. While outside the remit of CFR agencies, taxation plays a critical role in the competitiveness of Australia's financial system and is worth highlighting as an example in the context of considering Australia's competitiveness.

Australia's taxation settings are uncompetitive from a regional and international perspective, as evidenced by a headline corporate tax rate of 30% which is significantly higher than the OECD average. Additionally, Australia's taxation system includes frictions such as interest withholding tax which hinders the attraction of capital to Australia, which other jurisdictions either do not have or which operate in a more competitive manner. The un-competitiveness of Australia's taxation settings and recommendations to enhance the competitiveness were articulated in the 2009 Johnson Report into Australia as a Financial Centre; however, the bulk of the recommendations of the report remain unimplemented, notwithstanding apparent bipartisan support.

A prime example of the negative impact that tax can have on a financial centre's competitiveness was the 2021 repeal of the Offshore Banking Unit (**OBU**) regime. At a time when other countries, both regionally and globally, were actively enhancing and promoting their attractiveness as financial centres, Australia's relative attractiveness was significantly diminished in 2021 by the repeal of the regime. The OBU regime was a key pillar of Australia's financial centre attractiveness and, the regime's repeal ought to have been the catalyst for the Government to articulate the activities that it wishes to incentivise to retain and attract business to Australia and implement a regime that would do so. In the absence of incentives, participants operating in Australia that are competing for global business will face a tax rate of double their regional competitors.

4.1.1. Taxation and the ability of foreign banks to compete in Australia

A specific issue that faces foreign bank branches from a taxation perspective is Australia's idiosyncratic approach to the taxation of branches, referred to in taxation legislation as "permanent establishments." On the basis that branches are not separate legal entities, Australia's approach to determining the profits attributable to a foreign bank branch does not recognise internal dealings, that is, there is no ability for recognition of the taxation consequences of a transaction between the foreign bank branch and either head office or another part of the entity. This approach is out of step with both the latest OECD guidance and the approaches with most other jurisdictions, which recognise a "functionally separate approach" to branch taxation. This asymmetrical approach both adds complexity and increases the risk of double taxation, in circumstances where a payment from a foreign bank branch is treated as non-deductible in Australia and assessable in the recipient jurisdiction.

There is an elective tax regime for foreign bank branches (Part IIIB of the *Income Tax Assessment Act 1936*) which codifies a functionally separate enterprise approach; however, this regime also caps deductibility of internal funding costs under the LIBOR Cap, and hence is unattractive and also generates the potential for double taxation.

This demonstrates an example of how the construction of Australia's taxation regime results in foreign bank branches being taxed in an uncompetitive and complex way, with the approach not applying to Australian headquartered banks. This places foreign bank branches at a relative competitive disadvantage relative to Australian banks.