

Banking (prudential standard) determination No. 1 of 2022

Financial Sector (Collection of Data) (reporting standard) determination No. 11 of 2022

EXPLANATORY STATEMENT

Prepared by the Australian Prudential Regulation Authority (APRA)

Banking Act 1959, section 11AF

Financial Sector (Collection of Data) Act 2001, sections 13 and 15

Acts Interpretation Act 1901, section 33

Under subsection 11AF(1) of the *Banking Act 1959* (the Act), APRA has the power to determine a prudential standard in writing, which applies to all authorised deposit-taking institutions (ADIs) and authorised non-operating holding companies (authorised NOHCs). Under subsection 11AF(3) of the Act, APRA may, in writing, vary or revoke a prudential standard.

On 16 August 2022, APRA made Banking (prudential standard) determination No. 1 of 2022 (the APS 220 instrument), which revokes *Prudential Standard APS 220 Credit Risk Management* made under Banking (prudential standard) determination No. 2 of 2021 and determines a new *Prudential Standard APS 220 Credit Risk Management* (APS 220).

The APS 220 instrument commences on 1 September 2022.

Under subsection 13(1) of the *Financial Sector (Collection of Data) Act 2001* (the FSCODA Act), APRA has the power to determine reporting standards, in writing, with which financial sector entities must comply. Such standards relate to reporting financial or accounting data and other information regarding the business or activities of the entities. Subsection 33(3) of the *Acts Interpretation Act 1901* provides that where an Act confers a power to issue an instrument the power shall, unless the contrary intention appears, be construed as including a power exercisable in the like manner and subject to the like conditions (if any) to revoke any such instrument.

Subsection 15(1) of the FSCODA Act provides that APRA may declare a day on and after which the reporting standards are to apply.

On 22 August 2022, APRA made Financial Sector (Collection of Data) (reporting standard) determination No. 11 of 2022 (the ARS 233.0 instrument) which:

- (i) revokes *Reporting Standard ARS 223.0 Residential Mortgage Lending* made under Financial Sector (Collection of Data) (reporting standard) determination No. 6 of 2022; and
- (ii) determines a new version of *Reporting Standard ARS 223.0 Residential Mortgage Lending* (ARS 223.0).

The ARS 223.0 instrument commences on 1 October 2022.

1. Background

APRA's mandate is to ensure the safety and soundness of prudentially regulated financial institutions so that they can meet their financial promises to depositors, policyholders and fund members within a stable, efficient and competitive financial system.

APRA carries out this mandate through a multi-layered prudential framework that encompasses licensing and supervision of institutions. In the case of the banking industry, APRA is empowered under the Act to issue legally binding prudential standards that set out specific prudential requirements with which ADIs must comply. These standards are supported by prudential practice guides (PPGs), which clarify APRA's expectations with regard to prudential requirements. APRA collects data under reporting standards made under the FSCODA Act that enable APRA to assess ADIs' compliance with these prudential requirements.

APRA regularly reviews its regulatory regime and amends its prudential and accompanying reporting requirements as a result of a number of factors including:

- international developments;
- changes in financial market conditions or changes in risk management practices, in response to identified weaknesses in the prudential framework; and
- to reduce potential negative impacts of emerging industry issues.

One of the key components of APRA's prudential and reporting framework is the prudential standard that relates to an ADI's credit risk management and its accompanying reporting standards.

Prudential Standard APS 220 Credit Quality requires an ADI to control credit risk by adopting prudent credit risk management policies and procedures. Following a three month consultation period, APRA has updated APS 220 to include a new Attachment C which formalises APRA's toolkit of macroprudential policy credit measures. These are targeted policy tools which can be implemented or removed in response to systemic risks to the financial system.

During the consultation period, APRA also consulted on some small definitional changes to *Reporting Standard ARS 223.0 Residential Mortgage Lending* (ARS 223.0). These minor definitional changes have been made in response to ADIs seeking clarification and will ensure that industry takes a consistent approach to measuring macroprudential tools.

2. Purpose and operation of the instruments

The APS 220 instrument

The purpose of the APS 220 instrument is to revoke *Prudential Standard APS 220 Credit Risk Management* determination No. 2 of 2021 and replace it with a new version of the standard.

Where APS 220 refers to an Act, Regulation or prudential standard, this is a reference to the document as it exists from time to time, and which is available on the Federal Register of Legislation at www.legislation.gov.au.

APS 220 provides for APRA to exercise various discretions. Decisions made by APRA exercising those discretions are not subject to merits review. This is because these decisions are preliminary decisions that may facilitate or lead to substantive decisions which are subject to merits review.

A breach of a prudential standard is a breach of the Banking Act, as section 11AG of the Banking Act provides that ADIs must comply with applicable prudential standards. However, there are no penalties prescribed for breach of a prudential standard. Instead, an ADI's breach of a provision in the Act is grounds for APRA to make further, substantive decisions under the Banking Act in relation to the ADI. Those decisions may include the decision:

- (a) to revoke an authority to carry on banking business (section 9A of the Banking Act) and NOHC authorisation (section 11AB of the Banking Act); and
- (b) to issue a direction to the ADI, including a direction to comply with the whole or part of a prudential standard (section 11CA of the Banking Act).

It is only at this stage that an ADI is exposed to a penalty: loss of its authority under section 9A or 50 penalty units if it breaches the direction (section 11CG of the Banking Act). In nearly all cases¹ the decision is preceded by a full consultation with the ADI to raise any concerns it may have in relation to the decision.

The decisions of APRA to impose a direction are subject to merits review (section 11CA of the Banking Act) which is appropriately available at the point where an ADI could be exposed to a penalty.

Revocation of an authorisation to carry on banking business or a NOHC authorisation is subject to merits review unless either:

- (a) APRA has determined that access to natural justice and merits review is contrary to the national interest or contrary to the interests of depositors with the body corporate; or
- (b) the authority is an authority that is to cease to have effect on a day specified in the authority (section 9A(8) of the Banking Act).

The ARS 223.0 instrument

The purpose of the ARS 223.0 instrument is to revoke the existing ARS 223.0 and replace it with a new version of the standard, which requires ADIs to provide information to APRA about their businesses and activities. ARS 223.0 includes a reporting form that ADIs must complete and submit to APRA, and instructions to completing the reporting form.

¹ Subsection 9A(4) of the Act specifically provides that APRA does not need to consult where APRA is satisfied that doing so could result in a delay in revocation that would be:

- (a) contrary to the national interest; or
- (b) contrary to the interests of depositors with the ADI.

Where ARS 223.0 refers to an Act, Regulation, Prudential Standard, Reporting Standard, Australian Accounting Standard or Auditing Standard, this is a reference to the document as it exists from time to time, and which is available on the Federal Register of Legislation at www.legislation.gov.au.

There are a number of powers that may be exercised by APRA in reporting standards that involve an element of discretion and which may impact the interests of the financial sector entity to which the reporting standard applies. These decisions include APRA refusing to change a reporting period or due date for an ADI to provide information required by ARS223.0 or requiring foreign ADIs to report information required by ARS 223.0. Decisions made by APRA exercising those powers are not subject to merits review. These discretions have not been amended and are consistent with discretions included in the reporting standard being revoked by the ARS 223.0 instrument.

APRA considers decisions made by APRA exercising discretions under its reporting standards should not be subject to merits review as they are financial decisions with a significant public interest element.

APRA's reporting standards collect financial data from regulated entities. This data contains critical indicators of a regulated entity's financial wellbeing, including data on an entity's assets, capital, liquidity, expenses and risk exposures. APRA relies heavily on this financial data to inform its supervisory actions towards its regulated entities. Without timely and complete data, APRA may miss indicators that an ADI is taking on imprudent risk or is in distress. APRA's supervisory decisions may be jeopardised if its receipt of data is unreliable due to entities seeking merits review under its reporting standards.

The data collected by APRA's reporting standards is also often used to compile key macroeconomic indicators for Australia. The Reserve Bank of Australia uses the data to compile and publish its monetary and credit aggregates. The Australian Bureau of Statistics uses the data to compile the national accounts. The data is also used to meet Australia's international reporting obligations.

Delays caused by an entity seeking merits review of APRA's decisions under one or more reporting standards could significantly compromise these publications. As the publications are done at an aggregate level, any lack of data from one entity caused by a merits review claim prevents the release of the entire publication.

3. Consultation

On 11 November 2021, APRA undertook public consultation by way of a letter to all ADIs on the proposed changes to APS 220 and consequential amendments to ARS 223.0. As part of the consultation, APRA requested written submissions by 28 February 2022. APRA

incorporated stakeholder feedback into the final instrument, detailing its considerations and responding to submissions in a letter to all ADIs that was released on 14 June 2022.²

4. Regulation Impact Statement

The Office of Best Practice Regulation has advised that no Regulatory Impact Statement is required as the changes to APS 220 and ARS 223.0 are minor and machinery.

5. Statement of compatibility prepared in accordance with Part 3 of the Human Rights (Parliamentary Scrutiny) Act 2011

A Statement of compatibility prepared in accordance with Part 3 of the *Human Rights (Parliamentary Scrutiny) Act 2011* is provided at Attachment A to this Explanatory Statement.

² APRA Consultation - [Macprudential Policy: Credit Measures](#).

ATTACHMENT A

Statement of Compatibility with Human Rights

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

Banking (prudential standard) determination No. 1 of 2022 and Financial Sector (Collection of Data) (reporting standard) determination No. 11 of 2022

The legislative instruments 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* (HRPS Act).

Overview of the Legislative Instruments

The purpose of the instruments is to:

- (a) revoke the existing *Prudential Standard APS 220 Credit Risk Management* and replace it with a new version that includes a new attachment setting out APRA's credit-based macroprudential policy toolkit; and
- (b) revoke the existing *Reporting Standard ARS 223.0 Residential Mortgage Lending* and replace it with a new version that includes updated definitions for measuring APRA's macroprudential policy tools.

Human rights implications

APRA has assessed the instruments and is of the view that they do not engage any of the applicable rights or freedoms recognised or declared in the international instruments listed in section 3 of the HRPS Act. Accordingly, in APRA's assessment, the instruments are compatible with human rights.

Conclusion

The legislative instruments are compatible with human rights as they do not raise any human rights issues.