23 NOVEMBER 2022

ACTA – BANK TREASURY SIG

LATEST APRA DEVELOPMENTS FOR ADIs

JO DODD - PARTNER

60060206_1

White Clouds and Moon by Du Feichen

LATEST APRA DEVELOPMENTS

CAPITAL REFORMS

- APRA's new prudential standards for ADIs take effect on 1 January 2023
- Purpose is to ensure that ADIs are "unquestionably strong"
- New framework is to further strengthen the sector by ensuring that ADIs remain capitalised at the levels set in 2017
- To be effected by **ENHANCING FLEXIBILITY** (through higher capital buffers), **INCREASING CAPITAL REQUIREMENTS FOR HIGHER RISK LENDING** (and decreasing it for less risky lending), **SUPPORTING COMPETITION** (by limiting differences in capital requirements between smaller and larger banks), **IMPROVING THE COMPARABILITY OF BANK CAPITAL RATIOS** and **REDUCING THE OPERATIONAL BURDEN ON SMALLER BANKS** (by introducing simplified capital requirements for smaller, less complex banks)
- Framework was finalised in November 2021 – APRA recently released Prudential Practice Guides for APS 110, 112 and 113
- Consequential amendments around treatment of NZ exposures and NSFR
- APRA will allow ADIs to use temporary proxies to calculate capital requirements where data is unavailable

LATEST APRA DEVELOPMENTS

RESOLUTION PLANNING

- APRA released draft Prudential Practice Guides on financial contingency and resolution planning in September 2022: CPG 190 (Financial Contingency Planning) and CPG 900 (Resolution Planning)
- Principles and examples of best practice to assist APRA-regulated entities to meet the requirements under the proposed new prudential standards **CPS 190 Financial Contingency Planning** and **CPS 900 Resolution Planning** which APRA published in December 2021
- CPS 190 focuses on **minimising the RISK of entity failure** - will require all APRA-regulated entities to develop credible plans for managing stress that may threaten their viability
- CPS 900 is focused on **minimising the IMPACT of entity failure** - would require large or complex APRA-regulated entities to be organised so as to minimise risks to beneficiaries
- CPA 190 and 900 are proposed to take effect from 1 Jan 2024
- CPG 190 includes a number of statements of how APRA considers a “prudent” entity would approach the task of implementing an effective financial contingency plan

LATEST APRA DEVELOPMENTS

RESOLUTION PLANNING (CONT'D)

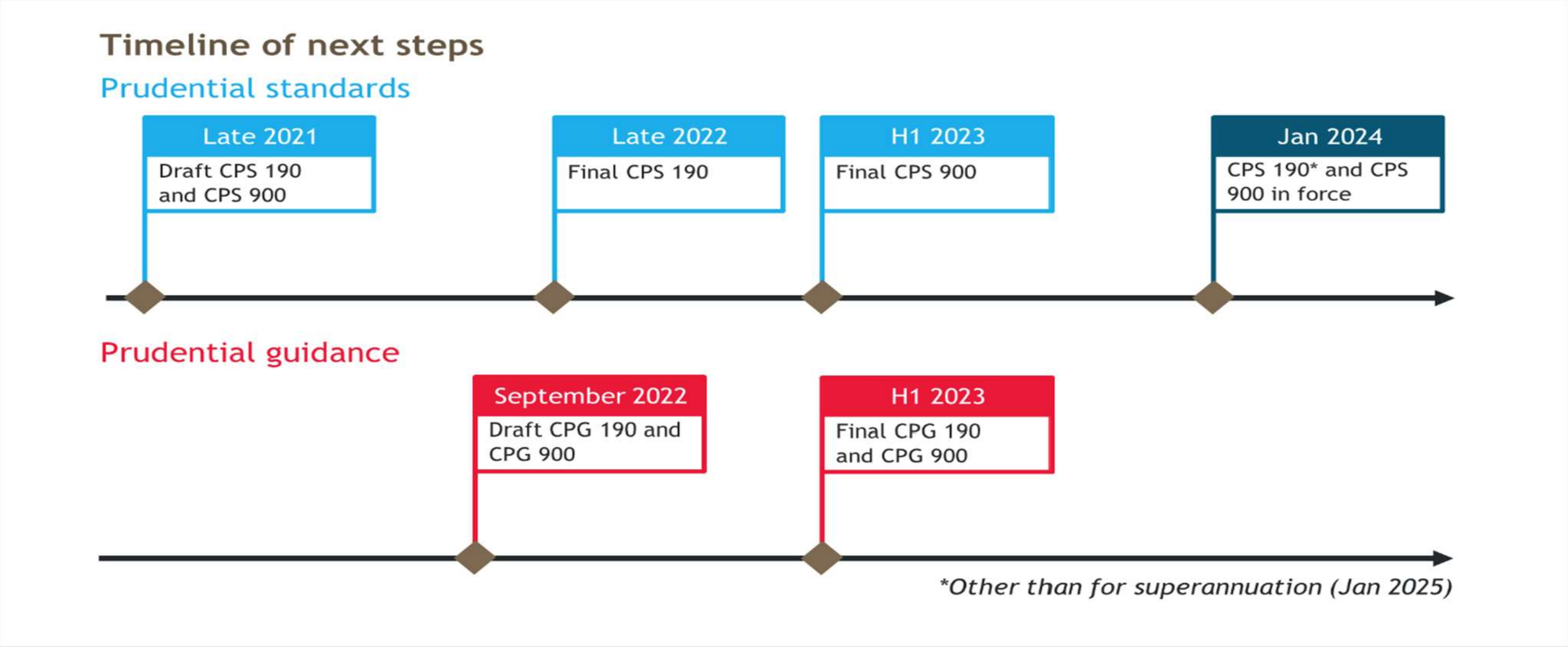
- CPG 900 establishes a framework through which regulated entities can engage with APRA to develop and implement a resolution plan, the execution of which ultimately lies with APRA
- APRA set out its views as to the appropriateness of resolution options for different kinds of entities in CPS 900. The application of some key potential options is shown in Table 1 below:

RESOLUTION OPTION	LIKELY APPLICATION	DESIRED OUTCOME
Recapitalisation	The largest and most complex entities, with significant critical functions	The conversion of hybrid capital instruments into equity, to restore viability using private, rather than public, funds
Transfer	Small to medium-sized entities, typically with limited critical functions	The transfer of all, or part, of an APRA-regulated entity to another party
Wind-down or run-off	Entities with no critical functions	Ceasing certain business activities with minimal adverse impact on customers, counterparties or the wider financial system

LATEST APRA DEVELOPMENTS

RESOLUTION PLANNING (CONT'D)

- Timeline for implementation:



LATEST APRA DEVELOPMENTS

CREDIT RISK REPORTING

- Proposed new Reporting Standards for prudential standards relating to capital adequacy and credit risk were released by APRA in April this year for consultation – APRA responded to submissions on them in August
- Concerns were raised around timing and the ability of ADIs to be able to comply by 1 Jan 2023
- APRA committed to 1 Jan 2023 implementation date but provided assistance with data collection and by holding information sessions
- Reporting treatment for exposures in NZ subsidiaries – APRA clarified that reporting is expected at Level 1 and Level 2 and that exposures in NZ subsidiaries are not to be included
- *ARS 118.1 – Other off-balance sheet exposures* discontinued
- First reporting date for *ARS 115 Capital Adequacy: Standardised Measurement Approach to Operational Risk* 35 calendar days after 31 March 2023
- Further information on Pillar 3 disclosure requirements also provided – APS 330 Public Disclosure. APS 330 to be finalised in 2022 with an effective date of 1 Jan 2024 – removal of disclosure requirements for smaller ADIs ('non-SFIs') being brought forward to 1 Jan 2023

THE COMMITTED LIQUIDITY FACILITY

- On 10 September 2021, APRA announced that it expected ADIs subject to the Liquidity Coverage Ratio to reduce their reliance on the Committed Liquidity Facility (CLF) to zero by the end of 2022
- LCR is a minimum requirement to ensure ADIs maintain sufficient unencumbered HQLAs to survive a severe liquidity stress scenario for 30 calendar days
- The CLF was established by the RBA in 2015 to compensate for the lack of sufficient HQLAs
- APRA and RBA now expect there to be sufficient HQLAs for ADIs to meet their LCR requirements without the CLF
- No ADI should be relying on the CLF to meet its minimum 100% LCR requirement (should have ceased from beginning of this year) – however ADIs could continue to count any remaining CLF as part of liquidity buffer
- CLF to reduce to zero by end of this year
- Third scheduled reduction occurred on 1 September 2022 (following planned reductions on 1 January and 30 April – final reduction to occur on 31 December)
- Aggregate CLF allocations are now approx. $33 billion (reduced from $66 billion on 1 May 2022)

LATEST APRA DEVELOPMENTS

RISK AND CULTURE

- *"No room for complacency on bank risk culture"*
- APRA risk culture survey conducted in late 2021 across 18 ADIs – all employees were invited to share their views on their ADI's risk management practices
- Overall, survey results show that work has been undertaken in ADIs to improve the communication and escalation of risk issues as well as establishing and monitoring of desired risk cultures – but also indicated that some of the tell-tale markers that contributed to the mismanagement of non-financial risks (as identified in the CBA Prudential Inquiry in 2018 and the subsequent Risk Governance Self-Assessments) are still prevalent
- Key insights:
- *Executives are overconfident regarding their entity's risk management capabilities*
- *Risk management practices vary widely*
- *Executives are prone to blind spots*
- *Risk management roles and responsibilities require further clarity*
- *Executives and individual contributors experience decision-making and constructive challenge differently*

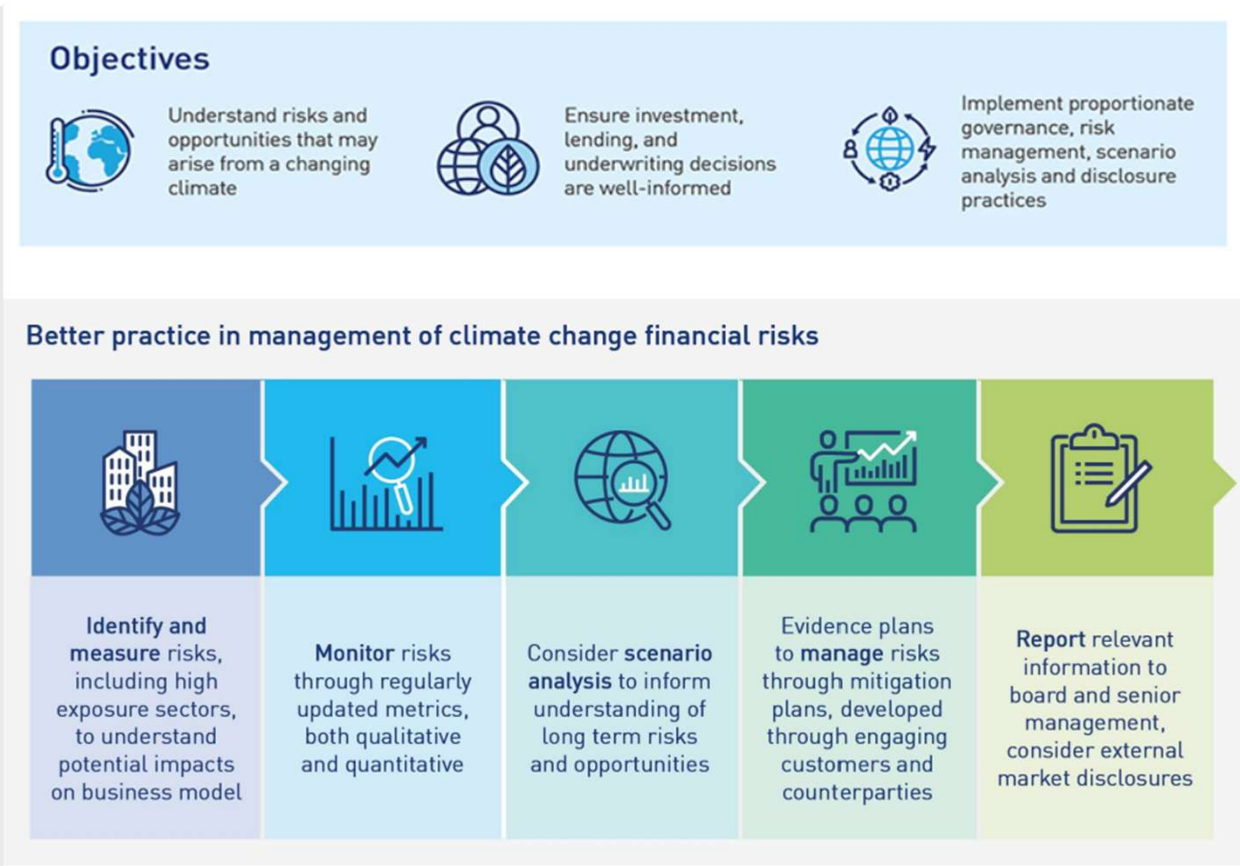
LATEST APRA DEVELOPMENTS

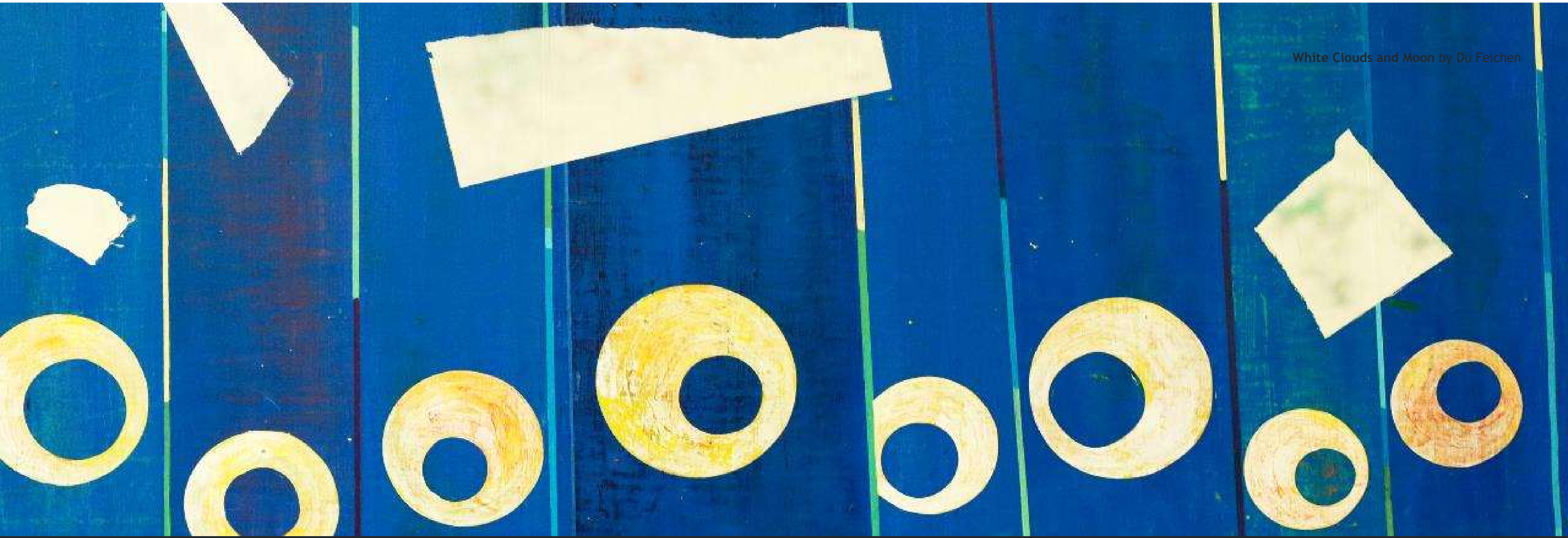
CLIMATE RISK

- Climate risk self-assessment survey conducted by APRA in March – results released in August
- Was designed to provide insights into how APRA-regulated entities are aligning their practices with the expectations set out in Prudential Practice Guide *CPG229 Climate Change Financial Risks* (released Nov 2021)
- 64 medium to large APRA-regulated entities participated in the survey: results suggest that they are generally aligning well to APRA's guidance, although only a small portion have fully embedded climate risk across their risk management framework
- CPG 229 is designed to assist banks, insurers and superannuation trustees to manage the financial risks of climate change – does not impose any new regulatory requirements or obligations, but is designed to assist entities to manage climate-related risks and opportunities within their existing risk management and governance practices (i.e. assist them in complying with the risk management and governance prudential requirements)

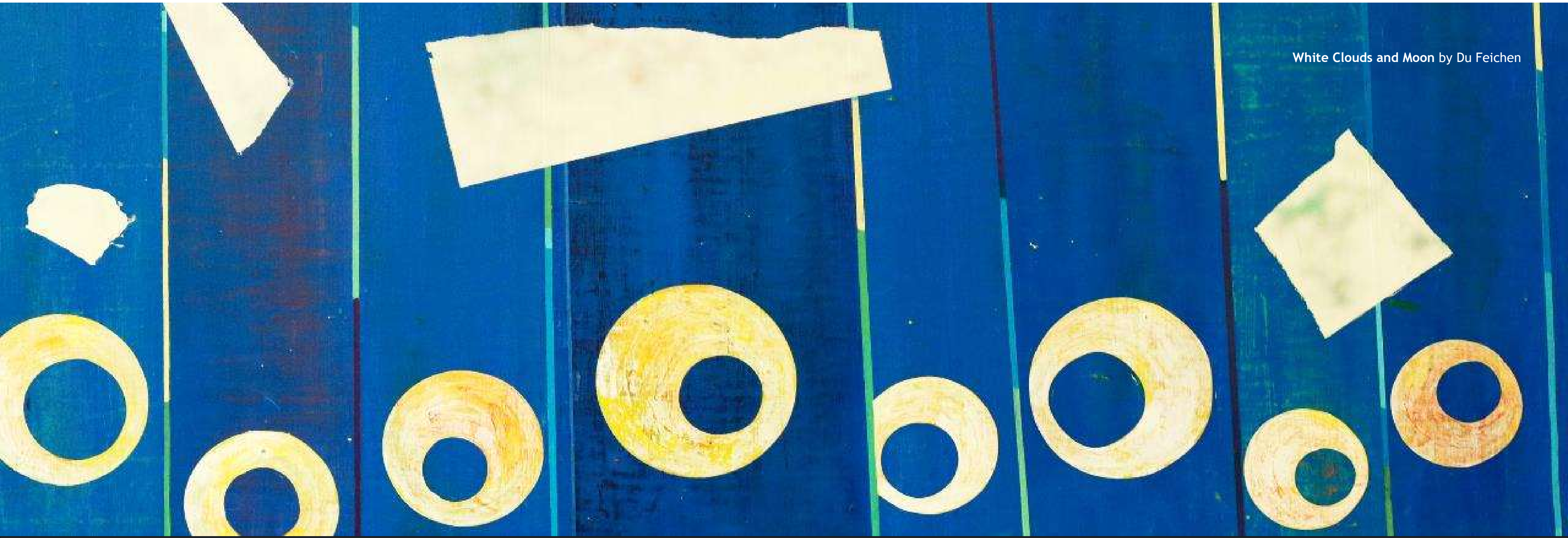
LATEST APRA DEVELOPMENTS

OVERVIEW OF CPG 229





THANK YOU


White Clouds and Moon by Du Feichen

QUESTIONS?