



14 March 2022

Mr Gideon Holland
General Manager, Policy Development
Australian Prudential Regulation Authority
By email

Dear Mr Holland

Revisions to the capital framework for authorised deposit-taking institutions: Draft Guidance

The Australian Banking Association (**ABA**) would like to thank the Australian Prudential Regulation Authority (**APRA**) for its ongoing engagement with industry in developing and implementing the revised capital framework. The ABA welcomes the opportunity to provide feedback on the draft guidance: Prudential Practice Guide APG 110 Capital Adequacy (**APG 110**); Prudential Practice Guide APG 112 Capital Adequacy: Standardised Approach to Credit Risk (**APG 112**) and Prudential Practice Guide APG 113 Capital Adequacy: Internal Ratings-based Approach to Credit Risk (**APG 113**).

Our position

The ABA continues to support a revised capital framework that strengthens the financial resilience of the industry, embeds the industry's unquestionably strong level of capital and provides for greater flexibility in periods of stress. ABA member banks are actively working towards the implementation of APRA's revised capital framework. Considerable work still remains in both defining and implementing the framework based on the practice guides issued as well as implementing related changes to regulatory reporting, modifications to Pillar 3 and international comparability studies, and updates to related standards.

The ABA and its members are committed to implementing the reforms and provide the attached comments to assist both the development of the guides and a unified understanding across industry of APRA's intent. Additionally, Appendix D contains questions on the implementation of the revised capital frameworks more broadly, while Appendix E provides additional information requested by APRA following a previous workshop with industry.

The ABA continues to work on a range of aspects of 'pragmatic implementation' of the reforms, including a set of industry wide proxies and assumptions. We look forward to iterative engagement with APRA as this work progresses.

Please contact me if you have any questions.

Yours sincerely

Brendon Harper
Policy Director



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- E. Additional information requested by APRA.



Appendix A: Issues and concerns

Topic	APRA Guidance	Issues/Impacts	Recommendations
<p>More than four Properties</p>	<p>APRA has proposed to include within the definition of IPRE exposures to individuals, family trusts or family companies where:</p> <ul style="list-style-type: none"> a) the exposure is for real estate investment or development purposes; b) prospects for debt servicing and repayment depend primarily on cash flows generated by real estate; and c) <i>the borrower has mortgaged more than four housing units (excluding the borrower's primary residence) with the ADI or other lenders. This information would be obtained at origination and updates on a best endeavours basis.</i> 	<p>The inclusion of retail customers with more than four housing units as IPRE exposures is problematic for the following reasons:</p> <ul style="list-style-type: none"> - Assessment Process: Existing assessment processes for retail clients, including frequency of collecting financial statements would not satisfy the non-retail requirements for the customer to be classified as IPRE. Assessment processes would need to be modified (for all relevant retail clients) to also collect collateral data of mortgages held with other ADIs, as customers are not required to disclose this today if it does not impact their loan application. - Rating Process: Existing rating processes for these customers are often aligned to retail modelling techniques such as account level, pool based modelling. New models would need to be developed to satisfy requirements for Non-Retail exposures. - Operational Complexity: The implementation is operationally complex as it requires an ADI to collect information on all loans and 	<p>APRA to allow customers with more than four residential properties to be classified as residential mortgage retail exposures. This is in line with the published Prudential Standards.</p> <p>APRA to ask ADIs to monitor the risks of 'more than four residential properties', on a best endeavours basis. Should the risks of this population appear to be:</p> <ul style="list-style-type: none"> - generating system-wide risks to financial stability, appropriate measures be considered, such as via APRA's macroprudential framework; or - inadequately captured by the existing models and capital framework, then industry to discuss with APRA an appropriate treatment once more information is known. This could include consideration within APS 220, whereby certain additional underwriting and customer management requirements could be considered.



		<p>security information behind those loans at other ADIs. Currently, ADIs do not always capture the security information linked to loans held with other financial institutions unless the security is applicable to the loan application.</p> <ul style="list-style-type: none"> - Customer Impacts: Customers may be required to provide more frequent financial information in order to meet Non-retail requirements such as annual reviews, provision of turnover data etc. This is a significant impost on the customer. In addition as the capital cost of the loans would increase, the pricing may change, which could drive the customers to Non-Bank lenders. 	
Bridging Loans	<p>For the recognition of a loan as Standard or Non-Standard, APG 112 states that the sale of a property may only be recognised as a factor in assessing a borrower's ability to meet their repayments in instances where there is a signed contract of sale that is due to be completed within six months of origination.</p>	<p>For Bridging Facilities, this would imply that most may not qualify for a Standard treatment.</p> <p>The proposal will require both Standardised and IRB ADIs to introduce additional processes for assessing, originating and managing bridging loan facilities, including the requirement that ADIs verify and capture details of whether the applicant is in possession of a signed contract of sale. This will introduce additional complexity, as such processes will need to address variations in property sale practices and settlement periods across each State,</p>	<p>That APRA allow for the sale of a property to be recognised as a factor in the assessment of a borrower's ability to meet their repayment obligations for all bridging facilities, with those bridging facilities that do not close within 12 months of origination to be classified as Non Standard loans. Such an approach would ensure that those bridging facilities that do not close within a reasonable period attract a higher capital charge under both the Standardised and IRB capital calculations.</p>



		<p>and the recognition of contracts of sale subject to any conditions.</p> <p>As only a small proportion of bridging loan applicants across the industry will likely qualify as 'Standard' loans, the proposals in the draft APG 112 will lead to an increase in the cost of bridging facilities for borrowers and could result in a tightening of the supply of credit to this segment of the market that primarily supports the transition of existing owner occupiers into another property.</p>	
Property backed Guarantees.	<p>For property exposures, under APS 112 (Attachment A, paragraph 13), "An ADI may use eligible CRM techniques to reduce the exposure amount of a property exposure, but the LVR band and applicable risk weight must be determined before the application of the relevant CRM technique."</p> <p>- Attachment A, paragraph 2 defines criteria for a guarantee to be eligible CRM and the new APS 112 contains other requirements on the use of CRM techniques (e.g. paragraph 18). APRA notes that unlimited guarantees are not permitted under the banking code of practice.</p>	<p>Family of the borrower can put a property backed guarantee in place to reduce the LVR of borrowers. These guarantees can either be limited to the property value, the exposure amount or limited to an amount specified.</p> <p>The suggestion to use CRM techniques does not work in this case because the standard (APS 112, Attachment I) permits a very different type of guarantor than the one in the question. For example, APS 112, Attachment I considers eligible guarantors being sovereigns, banks or other rated entities. That is very different from the family guarantee scenario which is actually fairly common across retail and SME customers.</p>	<p>To consider that a bank has security, comprising the property the bank is financing and the property provided by the other party.</p> <p>If the property provided by the other party meets the security conditions under APS 112 Attachment A then it could be included in LVR. In the view of industry, the fact that it is linked via a guarantee is secondary.</p> <p>ADIs presently include these third party mortgaged properties in its own LVR calculations and credit assessment, noting that the Code of Banking Practice contains strict compliance requirements for the taking of these mortgages.</p> <p>The ABA recommends that these forms of third party collateral be included in LVR calculations for purpose of APS 112 and APS 113.</p>



Topic	APRA Guidance	Clarifications Required	Recommendations
Countercyclical Capital Buffer (CCyB)	Paragraph 20 in APG 110 states “APRA does not expect ADIs to maintain operating targets above the capital buffer range in a severe stress scenario.”	<p>While APRA’s approach to the CCyB is outlined in the <i>Information Paper, The countercyclical capital buffer in Australia (December 2015)</i>, it does not provide specific guidance on the circumstances and triggers which would result in the default Australian CCyB being reduced to 0%.</p> <p>It is unclear to industry which specific triggers could change the default Australian CCyB of 1% and, as such, under which systemic stress scenarios, the release of CCyB can be assumed into their capital planning.</p>	APRA to consider updating its CCyB guidance on releasing CCyB with reference to paragraph 6.4 of the BCBS paper entitled “Range of practices in implementing the countercyclical capital buffer policy” (June 2017). Specifically, consideration should be had to introducing a structured quantitative approach to the release CCyB in order to reduce risk of asymmetric policy responses in times of stress and to provide more certainty to banks on the circumstances when CCyB will be released.
Land Acquisition, Development and Construction (ADC) Exposures	<p>In APS 112, APRA define ADC exposures as a collateral attribute dependent on the nature of the security to a loan.</p> <p>In APG 113, APRA’s indicative asset class mapping indicates ADC exposures are a subset of IPRE.</p>	<p>APRA’s definition of ADC is not necessarily consistent between APS 112, APG 113 and the draft Attachment C to APS 220 – a collateral attribute as defined in APS 112 is different to a repayment attribute as defined in APG 113/APS 220.</p> <p>Interpreting ADC as a sub-set of IPRE, for non-retail borrowers, will have the following benefits:</p> <ul style="list-style-type: none"> - promote consistency between the treatment of commercial property exposures between APS 112 and APS 113; 	APRA to align the guidance between APG 113, APS 112 and APS 220. The preference would be to have ADC as a subset of IPRE as the risks are higher for exposures where the repayment of the loan is dependent on the property and the collateral is under construction. The risks then would align with the higher proposed RW.



		<ul style="list-style-type: none"> - allow for IRB ADIs to utilise existing frameworks for identifying those borrowers reliant upon cashflows generated by real estate. Such an approach will ensure that facilities secured by land intended for development or property under construction attract a commensurately higher risk weight under the Standardised Approach to reflect that repayment will be dependent upon the future cashflows generated by assets still under development or other real estate holdings of the borrower; and - Conversely, the approach will ensure that facilities provided to general corporate borrowers secured by commercial property under construction, to be repaid from the borrower's broader commercial activities, will not be treated as ADC. 	
<p>SME Retail Requirements</p>	<p>APRA has indicated it has removed the requirement for all SME clients to provide financials, in line with current obligations for these clients. However, the wording of APS 113 and APG 113 imply that customers are still required to provide financials to justify their annual revenue is < \$75m to qualify as SME (updated at least every three years).</p>	<p>There are inconsistencies between the wording in APRA's information paper, the Prudential Standards and draft Prudential Practice Guides in regards to the requirements for financials for SME borrowers.</p>	<p>APRA allows ADIs to utilise data (other than consolidated revenue), existing processes (e.g. onboarding, origination, and review processes) and controls in ensuring that borrowers classified as SMEs are not connected to large corporate, financial institution or sovereign groups.</p> <p>APRA to align the wording between the information paper, the Prudential Standards</p>



			(APS 112/113) and Prudential Practice Guides (APG 112/113).
Covered Bonds (APS 113 Treatment)	APS 113 and the draft APG 113 do not specify the treatment of covered bonds under the IRB approach, including the assignment of supervisory LGDs.	<p>APS 113 and the draft APG 113 do not specify how covered bonds are to be treated under the IRB approach, including the assignment of supervisory LGDs to such exposures to Financial Institutions.</p> <p>Noting that a concessional risk weighting treatment for holdings of covered bonds under the Standardised Approach is detailed in Attachment B to APS 112.</p>	<p>APRA allows for ADIs to look-through to the assets in the cover pool in determining the supervisory LGD applicable to covered bond exposures.</p> <p>Where such pools are comprised of residential or commercial property exposures, recommend that APRA allows ADIs to utilise the supervisory LGDs applicable to exposures secured by eligible residential or commercial real estate.</p>

Criteria for recognition of 'other physical collateral'

Topic	APRA Guidance	Clarifications Required	Recommendations
<p>Definition of "Secured by immovable real property"</p> <p>APS 112, Attachment A; Paragraph 1</p>	<p>"A property exposure is an exposure that is secured by immovable real property."</p>	<p>Industry assumes this does not mean "fully" secured and, as such, proposes to identify property-secured under Paragraph 1 as follows:</p> <ul style="list-style-type: none"> All Retail mortgages; All Non-Retail facilities with IPRE ANZSICs; plus All Non-Retail facilities where valuation is equal to or exceeds exposure (i.e. is fully secured by property). Includes SBB also (SME Retail). 	<p>Attachment B contains the following risk weights to apply for borrowers that are not secured by property, are not externally rated, and not otherwise captured by other APS 112 asset class criteria:</p> <ul style="list-style-type: none"> Retail SME: 75% Corporate SME: 85% General Corporate: 100% <p>However, under Attachment A, Table 1, the risk weight for a Standard loan with LVR > 100% (no LMI) is in fact 105%. This</p>



			<p>means that, for example, a Retail SME business lending exposure that is only partly secured by property would be subject to a risk weight of 105%, whereas an equivalent Retail SME exposure that is wholly unsecured would get 75%. That is, the lodgment of part security (say a second registered mortgage over the business proprietor's home) would result in a materially worse risk weight outcome.</p> <p>It is for this reason that industry assumes that Attachment A only applies to fully secured property.</p> <p>ABA's thinking is that the 105% risk weight category in Table 1 was designed to capture Mortgages exposures where, say, the value of the residential property had declined (for example, a local town with industry concentration issues).</p> <p>In respect of commercial property, Attachment A Table 4 simply refers to Attachment B for high LVRs. As such, treatment will be the same as non-property secured anyway.</p>
<p>Definition of "E" for purpose of the LGD calculation under FIRB (General) and AIRB floor.</p>	<p>Where <i>E</i> is the current value of the exposure (i.e. cash lent or securities lent or posted)."</p>	<p>"E" for the LGD calculation is not well defined within the standards. Interpretations could include:</p> <ul style="list-style-type: none"> • Cash lent (as per the actual wording, which aligns to the Basel wording); 	<p>The ABA's expectation is that 'E' is EAD and the collateral for loans that have been accepted but not yet funded is based on "expected final collateral to be taken" as</p>



<p>APS 113, Attachment B, Paragraph 16</p>		<ul style="list-style-type: none"> Utilised limits; Total commitments; EAD; or Other? 	<p>opposed to “current perfected collateral”.</p>
<p>Credit Risk Mitigation (CRM) and “comparable direct exposure”: APS 113, Attachment B, Paragraph 49 Draft APG 113, Paragraph 47 (b)</p>	<p>“The application of CRM in the form of guarantees and credit derivatives must not reflect the effect of double default nor result in an adjusted risk weight that is less than that of a comparable direct exposure to the guarantor or credit protection provider.”</p>	<ul style="list-style-type: none"> The ABA notes that a “comparable direct exposure” to the guarantor or credit protection provider is usually an unsecured claim on the guarantor or credit protection provider. Under current practice, where a borrower has provided its own collateral, the RWA post-CRM may be less than a direct exposure to that guarantor, as the ABA has interpreted a “comparable direct exposure” to include the security offered by the obligor. 	<p>Industry believes that this (allowing also for the collateral) is a reasonable approach. It reflects the provision of both the collateral and the third party guarantee, which are each separate and additional supporting elements to the transaction. It applies across different portfolios, including larger corporates.</p>

Commitments

Topic	APRA Guidance	Clarifications Required	Recommendations
<p>Guidance for the recognition of commitments</p>	<p>In line with framework changes, APRA has changed the conditions which allow for facilities to be deemed uncommitted (Attachment C, Paragraph 3).</p>	<p>Further guidance is required to appropriately evaluate where certain facilities would be deemed ineligible for uncommitted treatment given the new conditions outlined in APS 112.</p>	<p>APRA to provide further guidance in what may be deemed as appropriate means of meeting the conditions outlined in APS 112, Attachment C, Paragraph 3. Specific recommendations are provided below.</p>
<ul style="list-style-type: none"> Fees and Commission – APS 112, Attachment C, Paragraph 3(a) 	<p>Per APS 112, “the ADI receives no fees or commissions to establish or maintain the arrangement.”</p>	<p>Clarification on what is deemed to meet the condition of a ‘no fees or commissions.’</p>	<p>Fees which are payable on drawdown (whether as a % of drawdown or nominal amount) are not considered fees to “establish or maintain the arrangement.”</p>



<ul style="list-style-type: none"> Assessment of creditworthiness – APS 113, Attachment E, Paragraph 7(d) 	<p>Per APS 112, “the ADI’s decision on the execution of each drawdown is made only after assessing the creditworthiness of the borrower immediately prior to drawdown;”</p>	<p>Guidance is sought on the conditions required to undertake credit assessments for the purposes of evaluating the credit worthiness of a counterparty prior to drawdown, including timing and materiality of such drawdowns.</p>	<p>The level of credit assessment required should be proportionate to the size of the drawdown, the time elapsed since the previous credit assessment and the amount of new information available since the prior credit assessment.</p> <p>For uncommitted asset-backed lending (e.g. warehouse facilities, borrowing base facilities), the assessment of creditworthiness may consist of customary checks of borrowing base calculation (e.g. financial covenant compliance, collateral coverage) by suitably qualified individuals.</p>
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PD Modelling

Topic	APRA Guidance	Clarifications Required	Recommendations
<p>Default Rate calculation</p>	<p>APRA’s new APG 113 provides further guidance on the calculation of default rates. Specifically, the proposed formulas require the removal of all exits</p>	<p>Identifying refinances can be difficult, as not all customer exit reasons are captured across all portfolios. For situations where ADIs cannot accurately identify refinancing within a portfolio, an alternative method of calculating default rates is to deduct <i>half of all exits</i>, regardless of whether the exit is due to a customer’s facilities maturing or being refinanced. This proposal is based on the theory that the denominator in the default rate calculation should take into consideration the length of time an obligor remains in the population regardless of exit reasons.</p>	<p>That APRA allow ADIs to adopt a simplification to the default rate formula by deducting half of all exits, where information is not available to determine if a customer has been refinanced or matured.</p>

Appendix C: Application of the Supervisory LGD framework to Large Corporates

The assignment of supervisory LGDs under APS 113 to exposures associated with infrastructure and regulated assets remains a topic where the industry would appreciate further guidance, with APRA requested to consider the following proposals:

Issue 1: Treatment of Infrastructure and Regulated Assets

APS 113 Attachment B – Paragraph 10 *“For senior exposures to operators of large public infrastructure assets or utilities that provide essential services to the economy, and have tripartite arrangements with Commonwealth or are valued on regulatory asset base”, an ADI must apply a 40% LGD where the operator is a corporate counterparty.*

Industry requests that APRA give consideration to the following:

1. Paragraph 10 of Attachment B to APS 113 is specific to unsecured, or the unsecured portion of, exposures to operators of large public infrastructure assets or utilities that provide essential services to the economy. Request for the concessional LGD to apply without a mandatory requirement of a “tripartite arrangement” in place and that this be reflected in APG 113, with an example provided in Attachment A.
 - Tripartite arrangements typically apply to secured exposures. It is an agreement between the borrower, lenders, and Government which recognises the lenders step-in rights. The tripartite recognises ranking of payments in the event that the concession/lease is sold following enforcement or step-in with financier’s claims ranking ahead of all others aside from any priority payments to the State.
2. Tripartite arrangements may be with Commonwealth or State Governments or offshore equivalents. In addition, a regulated asset base valuation refers to assets regulated via a domestic regulatory authority or offshore equivalent. Request that this be reflected in APG 113.
3. Financing of these transactions indicates a much lower LGD, reflecting the strong demand for these assets, which provide long term stable cash flows that appeal to local and international investment funds. If a supervisory LGD of 40% is adopted, this will heavily disadvantage APRA regulated ADIs compared to international competitors. Industry asks that APRA reconsider the 40% LGD for corporate counterparties.

Issue 2. Where these exposures are secured, industry proposes using the following treatment:

Collateral Type	Typical Security	Valuation Method	Proposed Treatment
Toll roads	- Generally secured by GSAs (fixed and floating charges) where the security includes charge over all relevant assets (including over the	- Discounted cash flow (“DCF”) over life of concession (based on internal valuation) - EBITDA sale multiples	FIRB asset classes: APS 113 Attachment B Table 5 - Eligible physical collateral 25% LGD



Collateral Type	Typical Security	Valuation Method	Proposed Treatment
	<p>concession/lease) and share mortgages.</p> <ul style="list-style-type: none"> - Guarantees - Security is also supported by a tripartite agreement between the borrower, lenders, and the Government (Commonwealth/State) which recognises the lenders step-in rights and priority ranking 		<p>AIRB asset classes: APS 113 Attachment B Table 6 - Other physical collateral 15% LGD floor</p> <ul style="list-style-type: none"> • Cash flows derive from control over physical collateral • Liquid market - Strong demand for infrastructure assets from global funds supports 25% LGD • Market price – valuations based on DCF • Perfected security interest via GSA and/or mortgage over lease • Right to inspect/examine linked to review event or event of default <p>Appendix C-2 below provides additional detail on how industry proposes that the eligibility criteria for 'eligible physical collateral' are met for the listed infrastructure collateral types.</p>
Airports	<ul style="list-style-type: none"> - GSA - Mortgage over the airport lease - Tripartite with the Commonwealth Government 	<ul style="list-style-type: none"> - Discounted cash flow over life of lease (based on internal valuation) - EBITDA sale multiples 	
Ports / Seaports	<ul style="list-style-type: none"> - GSA - Tripartite Deed with the Security Trustee, the borrower and the State in respect of the Lease - Mortgage over the lease 	<ul style="list-style-type: none"> - Leasehold improvements as per the audited accounts which are based on the mark to market value based on a DCF valuation - Discounted cash flow over the life of the lease (based on internal valuation) - EBITDA sale multiples 	
Rail	<ul style="list-style-type: none"> - GSA 	Leasehold improvements as per the audited accounts which are based on the mark to market value based on a DCF valuation	
Water	<ul style="list-style-type: none"> - GSA - Tripartite Deed with the Security Trustee, the borrower and the State Statutory 	Discounted cash flow over life of lease or Regulated Asset Base Value where regulated	



Collateral Type	Typical Security	Valuation Method	Proposed Treatment
	Corporation owners in respect of the Lease - Mortgage over the lease		
Electricity (regulated utilities)	- GSA - Tripartite Deed with the Security Trustee, the borrower and the owners in respect of the network Lease - Mortgage over the network lease	Regulated Asset Base value	
Public Private Partnerships (e.g. rail infrastructure, hospitals and other social infrastructure)	- GSA - Tripartite Deed with the Security Trustee, the borrower and the State in respect of the Lease - Mortgage over the lease	- Discounted cash flow over life of lease (based on internal valuation) - EBITDA sale multiples	

Issue 3: Treatment of residential and commercial properties on crown land

There are geographic regions where Crown land is predominant and freehold status is not available, for example residential and commercial property in the ACT and Sydney Harbour environs, and rural grazing land in QLD. Crown leases are typically very long term (up to 99 years) and, in the event of a sale, the lease is typically renewed for the new owner to provide certainty of possession. ADI's take a mortgage over the leases as collateral.

Industry proposes the following treatment of these mortgages:

- APS 112 Attachment A Paragraph 1 - Immovable real property
- APS 113 Attachment B Table 5 - Eligible residential real estate or commercial real estate
- APS 113 Attachment B Table 6 - Commercial or residential real estate

For the avoidance of doubt, this treatment would not be extended to other long-term leaseholds where freehold is owned by a private entity.

APPENDIX C-1

The below example reflects the proposed FIRB LGD calculation for a Corporate exposure to an infrastructure asset valued under a regulatory asset base.

Key Inputs:

Bank Value of Collateral

Type of collateral = Other Physical Collateral

Market Value of Collateral = \$100

APRA Prescribed Haircut = 40%

FIRB Bank Value of Collateral = \$60

EAD

Committed Loan Limit = \$100

Loan Utilisation = 100%

EAD = \$100

LGD Calculation

BV of Security = \$60

EAD of Secured exposure = \$60

Proportion of EAD that is secured = 60%

FIRB LGD on Secured Portion (Other Physical Collateral) = 25%

EAD of Unsecured Exposure = \$40

Proportion of EAD Unsecured = 40%

FIRB LGD on Unsecured Portion (infrastructure valued under a regulatory Asset Base) = 40%

Weighted Facility LGD = 31% (25% LGD x 60% + 40% LGD x 40%)

'Other Eligible Physical Collateral' – Eligibility Criteria (APS 113, Attachment E – Paragraph 7)

Eligibility Criteria	Industry Comments and Examples
<ul style="list-style-type: none"> <i>The ADI is able to demonstrate the existence of liquid markets for the disposal of collateral in an expeditious and economically efficient manner. The ADI must assess that this condition is being met both periodically and when information indicates material changes in the market.</i> 	<ul style="list-style-type: none"> ✓ The assets are considered of essential nature with monopolistic characteristics. Accordingly, they are highly sought after by both domestic and overseas investors, typically large pension funds. Data points are available with periodic sale of these of assets (generally sale of smaller equity stakes), although as investors are typically pension funds their preference is to hold the assets long term so there is less secondary market activity than for other collateral types.
<ul style="list-style-type: none"> <i>The ADI is able to demonstrate that there are well established, publicly available market prices for the collateral. For this purpose, publicly available market prices may include valuations from independent third-party appraisers that are available for purchase and reflect the current state of the market. The ADI must also be able to demonstrate that the amount it will receive when collateral is realised does not deviate significantly from these market prices.</i> 	<ul style="list-style-type: none"> ✓ There is sufficient public data on sale multiples of these assets. Given majority of these assets are ultimately owned by the State (or Commonwealth) there is also transparency of sales. ✓ Historical sale values haven been in line with, or stronger than, expected value, demonstrating strong demand. ✓ Valuations performed by a specialist appraiser who sits in the business but does not maintain a relationship with the client and is objectively reviewed, assessed and confirmed by an appropriately experienced and non-conflicted party would be considered independent. ✓ 'Publicly available market prices' may be established with reference to publicly available benchmark prices.
<ul style="list-style-type: none"> <i>The ADI must have a perfected security interest in the collateral, such that it has priority over all other lenders to the realised proceeds of the collateral. The security interest must be legally enforceable in all relevant jurisdictions, and the ADI must be able to realise the value of the collateral within a reasonable timeframe.</i> 	<ul style="list-style-type: none"> ✓ Security is clearly identified via Security Trust Deeds. ✓ Security generally includes charge over all relevant assets (including concession/leases via the asset owning entity) and share mortgages. ✓ Security is also supported by tripartite agreements between the borrower, lenders and the State which recognises lenders' step-in rights.
<ul style="list-style-type: none"> <i>The collateral is valued at no more than the current fair value under which it could be sold under contract between a willing seller and an independent buyer on the date of valuation.</i> 	<ul style="list-style-type: none"> ✓ There is sufficient public data on sale multiples of these assets. Given majority of these assets are ultimately owned by the State (or Commonwealth) there is also transparency of sales.



Eligibility Criteria	Industry Comments and Examples
<ul style="list-style-type: none"> <i>The ADI monitors the value of the collateral on at least an annual basis. More frequent monitoring is required where the market is subject to significant changes in value.</i> 	<ul style="list-style-type: none"> ✓ ADIs undertake periodic internal valuations for recovery analysis.
<ul style="list-style-type: none"> <i>the ADI must have clearly documented credit policies and procedures that detail the: (i) types of physical collateral accepted by the ADI, and policies and practices in respect of the appropriate amount of each type of collateral relative to the exposure amount;</i> <p><i>(ii) ADI's ability to liquidate the collateral readily; and</i></p> <p><i>(iii) ADI's ability to objectively establish a price or market value of the collateral, frequency with which the value can be readily obtained, and the volatility of the value of the collateral. The periodic revaluation process must pay particular attention to 'fashion-sensitive' collateral to ensure that valuations are appropriately adjusted downward for fashion, or model-year, obsolescence as well as physical obsolescence or deterioration.</i></p>	<ul style="list-style-type: none"> ✓ Dependent upon each ADI to maintain internal policies to address such requirements. ✓ There are sufficient historical data points on ADI's ability to liquidate with no restrictions.
<ul style="list-style-type: none"> <i>The ADI must have the right to physically inspect the collateral and have policies and procedures in place that set out the minimum frequency of inspection (physical or otherwise) for different types of collateral and the circumstances in which an inspection (physical or otherwise) of the collateral must be performed immediately.</i> 	<ul style="list-style-type: none"> ✓ Right to inspect/examine assets linked to review event or event of default. ✓ The concession/lease agreement between the State and the operator details the ongoing operating requirements, and the State can act on a breach of the Operator which automatically trigger a default on the Bank debt under the financing agreement. ✓ Security is clearly identified via Security Trust Deeds. There are sufficient data points in the market on the valuation of these assets. If deemed necessary by an ADI, it could carry out independent valuation of the asset. ✓ Where clear legal title is held to assets, this criterion is satisfied provided there are no impediments to examining or revaluing the collateral at the discretion of the ADI.



Eligibility Criteria	Industry Comments and Examples
<ul style="list-style-type: none"><i>The ADI ensures that the collateral is adequately insured.</i>	<ul style="list-style-type: none">✓ Appropriate insurance is required to be taken by the borrowers, with such requirements typically documented under financing agreements. The renewal of insurance is reconfirmed per financing arrangements.
<ul style="list-style-type: none"><i>The ADI monitors the risk of environmental liability arising in respect of the collateral.</i>	<ul style="list-style-type: none">✓ As addressed through ADI's internal policy and risk management frameworks. Noting that borrowers are typically required to comply with relevant Environmental Laws under the financing documents, with any breaches to be reported.



Topic	APRA Guidance	Issues/Impacts	Recommendations
Roadmap to 2023	APRA has issued new prudential standards to the industry and draft prudential practice guides in November 2021. APRA intends to progress revisions to associated reporting requirements and other related standards in 2022 to prepare the industry for implementation on 1 January 2023	<ul style="list-style-type: none"> - There will need to be changes to related standards in order to comply with the new framework and avoid adverse impacts. Examples include changes to the Liquidity standard (APS 210) and Residential Mortgages (APG 223). - Given the tight implementation timeframes, the industry would appreciate an update to APRA’s roadmap to 2023 with timelines on when it would expect to receive the revisions to other prudential standards, and the timelines for implementation 	<p>APRA to publish an updated roadmap which outline its plans on:</p> <ul style="list-style-type: none"> - Prudential visits to discuss the implementation of the reforms; - Changes to related standards and implementation dates; - Updates to Regulatory Reporting, inclusive of any pilot exercises and ‘parallel runs’; and - International Comparability studies.
Pillar 3	APRA is not intending to update Pillar 3 requirements until 2024.	<ul style="list-style-type: none"> - There will be a period of 1 year where ADIs will be required to disclose new capital requirements externally using existing APS 330/Pillar 3 standards which may not be fit for purpose for the new capital standards. - Flexibility in the Pillar 3 requirements is needed to ensure clear and transparent disclosures, easier implementation for ADIs (that is not needing to fit concepts designed for the current standards using the new standards) and will avoid ADIs needing to maintain concepts that apply to the prior standards. - Public guidance on Pillar 3 is required from APRA to ensure that External Audit and 	APRA to provide public guidance on its plans for Pillar 3.



		APRA assurance requirements on reporting can be met.	
Reporting	APRA has not begun formal consultation on the reporting requirements and changes to existing reporting as part of the implementation of the new capital standards.	<ul style="list-style-type: none"> - Given the volume of change required in ADIs to achieve compliance with the capital standards by 1 January 2023 timelines, large changes to reporting requirements would put a high amount of burden on a limited set of SMEs, which may result in delays or suboptimal implementations. - APRA only intend to consult on reporting changes in March 2022, which provides ADIs with less than 12 months to implement the new reports. 	<p>ADIs would appreciate if APRA could undertake the following:</p> <ul style="list-style-type: none"> - Provide a clear roadmap with detailed requirements on the upcoming changes to regulatory reporting - Provide a set of FAQs which provide more detailed guidance on definitions and APRA's requirements for reporting - Limit the amount of changes required for interim reporting to allow more time to focus on the capital implementation; - Limit the amount of changes required as part of pilot processes until the capital changes are implemented.
International Comparability	APRA will be issuing a study on international comparability in 2023.	<ul style="list-style-type: none"> - Internationally Harmonised numbers will need to be disclosed by ADIs once the new standards are in effect on 1 January 2023. As APRA is not intending to commence its internationally harmonised study until 2023, there will be a period where ADIs are disclosing harmonised numbers based on their own best judgment of differences to the international framework. - Without consistent adjustments and an endorsed independent study, these disclosures are not likely to be meaningful. 	ADIs would appreciate if APRA could provide guidance on internationally harmonised disclosures before 1 January 2023. This could include the pausing of such disclosures until an APRA study is published or endorsing an industry led consistent approach.



Appendix E: Additional information requested by APRA

The following information is provided in response to previous requests from APRA for additional information relating to the revised capital framework.

1) Standard loan classification (predominant and make weight security) – ABA questions #9/APRA response #5:

- **ABA's question:** Based on APS 112 and the draft APG 112, if it meets various conditions, an exposure can be treated as a standard loan including where an exposure is secured by multiple types of collateral which would include:

1. a predominant unequivocal enforceable first mortgage over property ABC; and

2. a make weight security to improve LVR lending position through a second mortgage of property XYZ that would not meet the requirements of 'standard loan' under APS112 Attachment A Para 4(a)-(d).

Can APRA confirm that status of a 'standard loan', in the above example, is not altered by the inclusion of the second mortgage?

- **APRA's response:** APRA requests that ABA members provide more information on the materiality of this issue. In addition, APRA would like to understand the types of loans where this practice may be applied.

Additional information: This scenario will happen occasionally in Mortgages. A typical scenario is where a parent provides their own home as supporting security for their child's financing of their first home (to reduce the overall LVR and potentially avoid LMI in the process). That home owned by the parent might have a pre-existing mortgage from the parent's lender, which could be from a different ADI. It is then unclear (assuming a bank is able to improve the LVR through this third party security in the first place), does the fact that the supporting security is a 2nd ranking mortgage make the whole loan Non-Standard?

2) Commitments and "other constraining factors" – ABA question #15/APRA response #7:

- **ABA's question:** In question 15 of the ABA letter of 8 December, industry have queried if paragraph 33 of the new APS 113 would apply where: the overall commitment might be say \$100m, with \$10m available initially based on the provision of say \$15m in collateral "up-front". That is, could an ADI record the lower value as a commitment given the constraining factor on availability of the facility.

- **APRA's response:** APRA requests that ABA members provide further information on this example to confirm the constraints around the process and if the limit on the facility formally changes from \$100m to \$10m.

Additional information: The issue being considered is not the facility changing from \$10m to \$100m. The documented commitment could be \$100m, but in many cases this will be drawn at different amounts (the drawn amount may go up and down over time). The \$100m commitment represents the maximum the bank will allow the drawing to go to. The key point is that all drawings are subject to the provision of supporting collateral (for example, maintenance of a maximum LVR on property collateral). Thus, at any time the customer can only draw up to that LVR based on the collateral held. This amount may be (materially) less than the overall \$100m commitment.