

House of Representatives Standing Committee on Economics

ANSWERS TO QUESTIONS ON NOTICE

Review of the Australian Prudential Regulation Authority Annual Report 2023

Agency: Australian Prudential Regulation Authority
Question No: APRAQW7
Topic: Lessons learnt for the banking sector
Reference: Written (4/11/2024)
Member: Mr Bert van Manen MP

Question:

Within your latest Corporate Plan 2024-25, one of your top priorities is to reflect lessons learnt for the banking sector by strengthening bank capital and liquidity standards. Can you expand on what these standards might be?

Answer:

On capital, APRA is proposing to update the bank capital framework to strengthen crisis preparedness. Specifically, APRA is proposing that banks phase out the use of AT1 capital instruments (often called hybrid bonds) and replace them with cheaper and more reliable forms of capital that would absorb losses more effectively in times of stress. The total amount of regulatory capital that APRA requires banks to hold would remain unchanged and banks would remain 'unquestionably strong'. APRA's proposal is detailed further in our Discussion Paper of 10 September 2024.¹ APRA plans to provide an update on the consultation process in late 2024.

On liquidity, APRA in July 2024 released finalised targeted changes to strengthen banks' liquidity and capital requirements.² In the response paper that accompanied APRA's public release, APRA confirmed we would undertake a broader review of liquidity risk as planned.³ APRA's response paper also indicated some areas expected to be in scope, such as avenues to promote liquidity resilience in a more cost-effective way, the appropriate calibration and design of liquidity requirements, and potential changes to eligible liquid assets. In terms of timing, the next step will be industry engagement in H1 2025. Public consultation on a discussion paper would follow, although this is not planned for FY2024-25. In proposing potential changes, APRA will per our statutory mandate give consideration to financial safety and financial stability, balancing efficiency and competition.

A further lesson learnt through last year's international banking crisis was the importance of banks prudently managing interest rate risk in the banking book (IRRBB). While APRA's long-standing supervisory and policy approach to IRRBB held the Australian banking system in good stead avoiding the experience of some overseas banks, APRA in July 2024 finalised some prudential standard changes.⁴ The changes create better incentives for ADIs to manage IRRBB and simplify the IRRBB framework to enhance proportionality across ADIs.

¹ <https://www.apra.gov.au/a-more-effective-capital-framework-for-a-crisis>.

The discussion paper lists the prudential standards that would be affected, the main standards being:

- Prudential Standard APS 110 Capital Adequacy
- Prudential Standard APS 111 Capital Adequacy: Measurement of Capital
- Prudential Standard APS 221 Large Exposures
- Prudential Standard APS 222 Associations with Related Entities

² <https://www.apra.gov.au/news-and-publications/apra-finalises-targeted-changes-to-strengthen-banks%E2%80%99-liquidity-and-capital>.

³ The main prudential standard that would be affected would be Prudential Standard APS 210 Liquidity.

⁴ Prudential Standard APS 117 Capital Adequacy: Interest Rate Risk in the Banking Book (APS 117).

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Agency: Australian Prudential Regulation Authority
Question No: APRAQW8
Topic: Macroprudential tools
Reference: Written (4/11/2024)
Member: Mr Bert van Manen MP

Question:

APRA made the decision to leave the serviceability buffer unchanged at 3.0 percentage points and the countercyclical capital buffer at 1.0% of risk weighted assets throughout 2023-24 to maintain lending standards. Can you explain if this practice is still beneficial for borrowers given the interest rates are sitting at over 5-6%?

Answer:

APRA's primary purpose is to ensure the safety and stability of the Australian financial system. A stable financial system is essential for a thriving and dynamic economy, and benefits all Australians.

APRA sets macroprudential policy with an aim to mitigate risks to financial stability at a system-wide level. This includes three core tools – the serviceability buffer, the countercyclical capital buffer and limits on bank lending – that work together to ensure that banks are making sound decisions and are calibrated to promote resilience and promote credit availability in times of stress. We take into consideration what we are seeing in the financial system, as well as monetary policy settings, the economic environment and factors that could impact financial stability such as geopolitical instability. APRA regularly reviews its macroprudential policy settings throughout the year, and in doing so liaises closely with Council of Financial Regulator colleagues, including the Reserve Bank of Australia.

Serviceability assessment buffer

The serviceability buffer exists to ensure that banks lend to borrowers an amount which supports their ability to repay in a range of scenarios. The buffer provides an important contingency for a range of future economic shocks – not only for rises in interest rates – over the life of the loan. It also factors in unforeseen changes in a borrower's income or expenses, which we have seen play out recently as cost-of-living pressures mount. These shocks can relate to an individual household's life circumstances, such as an unforeseen illness, or a change in economic developments such as increases in interest rates, rising cost of living, or a weakening labour market.

The setting also accounts for risks to the financial system associated with Australia's high overall household indebtedness and rising housing-related vulnerabilities. Over the past 20 years, household debt-to-income has risen from around one and a half times income to around two times. Yet, in percentage terms, APRA-regulated banks have more housing loans on their books than most other comparable countries. Around two-thirds of all loans are for housing in Australia.

The serviceability buffer is calibrated at the system-wide level and so is not likely to be appropriate for every lending decision. Therefore, these policy settings also allow for flexibility – banks are able to make exceptions on a case-by-case basis where it is prudent to do so. This enables the system to remain responsive to the varied needs of borrowers and their individual circumstances without compromising stability.

Countercyclical capital buffer (CCyB)

The countercyclical capital buffer (CCyB) (which has a default setting of 1 per cent of risk-weighted assets) provides flexibility in times of stress: it can be reduced where the flow of credit has been disrupted to ensure the banking sector can absorb losses and continue to lend to support households and businesses when they most need it.

Current settings

In July, APRA confirmed that it would maintain the serviceability buffer at 3 percentage points above the loan rate and the CCyB at its default setting of 1 per cent. In reaching this decision, APRA considered the uncertain interest rate and economic outlook, with underlying inflation still above the Reserve Bank of Australia's target range, as well as ongoing geopolitical instability. APRA noted that the quality of new housing lending remained sound, and while arrears rates on mortgage and business lending portfolios have continued to rise slowly, they remained below Covid peaks.

Credit was flowing and accessible, with credit growth for home purchases a little below its long-term average. High debt-to-income and high loan-to-valuation ratio lending made up only small proportions of new lending. Lending standards remained sound with banks able to make exceptions to their serviceability policy if prudent to do so. Given the uncertain economic and interest rate outlook, including the possibility of higher cost-of-living pressures, it was important that prudent buffers remained in serviceability assessments.

APRA is carefully monitoring financial conditions and will adjust macroprudential settings if necessary.

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Agency: Australian Prudential Regulation Authority
Question No: APRAQW9
Topic: Freedom of Information Requests
Reference: Written (4/11/2024)
Member: Mr Bert van Manen MP

Question:

On 20 August 2024, the Committee was copied into an open letter to the Senate Economics Committee from John Telford of Victims of Financial Fraud, stating that Section 38 of the Freedom of Information Act and Section 56 of the APRA Act ‘act as a fortress, keeping the public away from discovering facts’. On the Disclosure log APRA had 7 FOI requests; 4 of the 7 had data only partially released. Can you outline to what extent section 56 of the APRA Act applied for the release of those matters?

Answer:

Section 56 of the APRA Act and section 38 of the *Freedom of Information Act 1982* (FOI Act) did not apply to any of the documents that were partially released in response to the four FOI requests referred to in the Question above. The information that was not released in the partially released documents was redacted on the basis that it was irrelevant to the respective FOI requests, pursuant to section 22 of the FOI Act.

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Agency: Australian Prudential Regulation Authority
Question No: APRAQW10
Topic: Retirement Outcomes
Reference: Written (4/11/2024)
Member: Mr Bert van Manen MP

Question:

Can you outline your work with superannuation trustees in supporting their members entering retirement?

Answer:

APRA is focussed on trustees' implementation of the retirement income covenant which came into effect in July 2022.

Jointly with ASIC, we undertook a thematic review into the progress being made by trustees to implement the retirement income covenant, the findings for which were published in July 2023.¹ Overall, the review found that while trustees are improving their offerings of assistance to members in retirement, there is variability in the quality of approach taken and a lack of urgency in embracing the intent of the covenant.

A follow-up pulse check conducted by APRA and ASIC in November 2023 and published in July 2024, showed progress had been made, although not in the critical area of tracking and measuring the success of trustees' retirement income strategies.²

To maintain supervisory focus on implementation of the covenant, as noted in our 2024-25 Corporate Plan, APRA will:

- continue to work with ASIC to monitor and use supervisory activities to drive industry to improve retirement outcomes and customer experience of superannuation members;
- hold individual trustees to account where APRA holds concern about lack of progress being made to effectively implement the retirement income covenant; and
- continue to engage with life insurance industry to explore ways to reduce barriers for insurers to provide and/or further innovate longevity solutions.

In parallel, APRA has embedded requirements relating to retirement in its prudential framework through updates to Superannuation *Prudential Standard SPS 515 Strategic Planning and Member Outcomes*. This includes amendments to reflect heightened expectations of trustees in embedding the requirements of the retirement income covenant within their existing strategic and business planning practices, reviewing the outcomes achieved and taking action where objectives are not achieved.

¹ <https://www.apra.gov.au/information-report-implementation-of-retirement-income-covenant-findings-from-joint-apra-and-asic>.

² <https://www.apra.gov.au/industry-update-pulse-check-on-retirement-income-covenant-implementation>.

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Agency: Australian Prudential Regulation Authority
Question No: APRAQW11
Topic: Governance, Culture and Accountability
Reference: Written (4/11/2024)
Member: Ms Tania Lawrence MP

Question:

ANZ provided APRA with its self assessment on government, culture and accountability. Does APRA intend to make this report public? If so, when? If not, why not?

Answer:

Following the release of the final report of the Prudential Inquiry into the Commonwealth Bank of Australia (Inquiry) in May 2018, APRA wrote to the Boards of several large regulated entities, including ANZ, to request a self-assessment to assess if similar issues identified through the Inquiry were present in their organisations.

While these entities, including ANZ, have provided copies of their self-assessment reports to APRA, these reports belong to the entities, and it is the individual entity's decision as to whether it makes the report public. These self-assessment reports are protected information under section 56 of the APRA Act.

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Agency: Australian Prudential Regulation Authority
Question No: APRAQW12
Topic: Disqualification decisions: Banking
Reference: Written (4/11/2024)
Member: Ms Tania Lawrence MP

Question:

1. How many disqualification decisions were made in relation to the banking industry during 2022/23?
2. How many proceedings for disqualification were commenced by APRA in that period in the Federal Court in relation to the banking industry?
3. Please also indicate whether information in relation to action taken for disqualification under the Financial Accountability Regime Act 2023 will be provided in future annual reports.

Answer:

1. 0
2. 0
3. In its Annual Report, APRA typically provides an overview and summary of its enforcement activity during the year. APRA reports enforcement activity at an aggregate level and does not report on enforcement activity against specific statutes. Any action APRA takes for disqualification under the *Financial Accountability Regime Act 2023* would be included in APRA's Annual Report.

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Agency: Australian Prudential Regulation Authority
Question No: APRAQW13
Topic: Bank Bill Swap Rate Litigation
Reference: Written (4/11/2024)
Member: Ms Tania Lawrence MP

Question:

For how many of the accountable persons involved in the Bank Bill Swap Rate litigation, such as Shayne Elliott, the current CEO of ANZ, was disqualification (a) considered and (b) pursued?

Answer:

APRA is subject to secrecy provisions under the APRA Act and accordingly cannot reveal any information relation to individual accountability assessments, if any, that have been undertaken in relation to an APRA-regulated entity. Consistent with APRA's enforcement approach¹, APRA considers when and how it will publicise the enforcement actions it takes on a case-by-case basis. Unless there are likely to be risks to beneficiaries' interests and / or financial stability from publicising an action, APRA will typically publicise enforcement actions taken by APRA, such as: formal directions and licence conditions or infringement notices; acceptance of an enforceable undertaking received from a regulated entity or an individual; disqualifications of accountable persons under the Bank Executive Accountability Regime or the Financial Accountability Regime, or other responsible persons under the prudential framework; and court-based enforcement actions commenced by APRA.

¹ <https://www.apra.gov.au/enforcement>.

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Agency: Australian Prudential Regulation Authority
Question No: APRAQW14
Topic: Disqualifications
Reference: Written (4/11/2024)
Member: Ms Tania Lawrence MP

Question:

1. Where there are repeated failures by an entity to comply with APRA requirements, is disqualification of accountable persons considered?
2. Where a litigation is settled prior to trial, does settlement have any bearing on whether APRA seeks disqualification of accountable persons? Has this been part of any settlement negotiations or agreement?

Answer:

1. APRA's enforcement approach¹ sets out the basis on which APRA will consider whether to take enforcement action. We dedicate our resources to those matters which will have the greatest regulatory impact informed by the following guiding principles:
 - a. Risk-based: APRA's appetite for enforcement should prioritise the issues and entities that pose the most serious prudential risk;
 - b. Forward-looking: APRA should use enforcement to prevent serious prudential risks from having a realised impact;
 - c. Outcomes-based: APRA should use enforcement when appropriate to achieve desired prudential outcomes; and
 - d. General and specific deterrence: APRA should actively consider the need to deter similar practices from occurring in the future.

Individual accountability is an important part of the regulatory toolkit and will be a strong consideration when weighing up the above factors. Individual accountability will be considered both at the outset of, and during, regulatory investigations.

2. As set out above, APRA's enforcement criteria are the main tool we use to determine what enforcement action, if any, APRA should take in a particular set of circumstances. This will include, at the outset of an investigation and on an ongoing basis, individual accountability. Where APRA is considering taking action, it carefully considers the facts as established by extensive investigation and this is the primary mechanism through which culpability of an individual will be established.

¹ <https://www.apra.gov.au/enforcement>.

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Agency: Australian Prudential Regulation Authority
Question No: APRAQW15
Topic: Insurance in super
Reference: Written (4/11/2024)
Member: Ms Tania Lawrence MP

Question:

Some Superannuation Funds have a default setting whereby insurance premiums for life and TPD are charged at a higher, nominally blue collar rate unless members actively apply for a lower, white collar or professional rate. This has occurred notwithstanding that when members join super funds, they fill in details of their employment, so in fact the super fund has already received notice of their type of employment. Members who should have been charged at the cheaper rate have arguably been wrongly disadvantaged to the tune of hundreds of dollars, plus investment returns/interest foregone.

Does APRA have an attitude to this practice? Has it taken any action or given any advice to super funds in relation to this? Is legislation needed to correct it?

Answer:

Trustees are required under the current legal framework to be able to demonstrate their insurance in super settings result in the fair and equitable treatment of members.

APRA's prudential requirements and guidance is contained in *Prudential Standard SPS 250 Insurance in Superannuation* (SPS 250) and *Prudential Practice Guide SPG 250 Insurance in Superannuation* (SPG 250). SPG 250 expressly states that:

58. SPS 250 requires an RSE licensee to be satisfied, and to be able to demonstrate to APRA, that the rules for attributing any status to a beneficiary, cohort or class of beneficiaries, in connection with the provision of insurance, are fair and reasonable.

59. APRA considers that 'fair and reasonable' in this context would require that the rules that apply to an RSE licensee or an insurer would be applied in an equitable manner to take into account the financial impact of attributing a particular status to a beneficiary, cohort or class of beneficiaries. This is particularly important where it may affect the premium to be charged for insurance. For example, a status such as occupation class/type of 'blue-collar' or 'white collar'... affects the premium to be charged. In determining whether a rule to attribute a status to a beneficiary is 'fair and reasonable', a prudent RSE licensee would be able to demonstrate that the rules for attributing a particular status to a particular beneficiary, cohort or class of beneficiaries are based on statistically appropriate data, sourced from the RSE's own data where there is sufficient data available.

APRA wrote¹ to the industry in December 2023 noting the importance of insurance in super and highlighted the need for insurance offerings to be sustainably designed and priced, to

¹ <https://www.apra.gov.au/sustainability-of-life-insurance-superannuation-december-2023>.

provide outcomes that are of value to members, and the importance of data quality (including occupation data) in the design and pricing of insured benefits.

APRA's supervision is focused on ensuring the industry meet these requirements to support the best possible outcomes for their members. APRA strongly encourages RSE licensees, life insurers and reinsurers to work together to obtain data to ensure that the default insurance offering is appropriate for the insurance needs of member cohorts.