Australian Banking Association

03 December 2020

Mr Ben Mowatt
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By email Ben.mowatt@Apra.gov.au

Dear Mr Mowatt

ABA approach to implementing APS 222

The revised Prudential Standard APS 222 *Associations with Related Entities* (**APS 222**) will become effective from 1st January 2022. A number of the changes to APS 222 will require a significant lead time for banks to implement.

The purpose of this letter is to inform APRA of the Australian Banking Association's (**ABA**) approach to the implementation of the following requirements in the revised APS 222 ahead of our APS 222 workshop on 9 December 2020. The ABA approach to the following requirements is set out in the attached:

- Step-in risk entities
- Exposures to related entity securitisation and covered bond special purpose vehicles
- Related entities and related entity funds
- Extended licensed entity (**ELE**) subsidiaries; and
- Regulatory reporting.

The ABA's aim is to ensure a consistent approach to compliance is taken, to enable robust processes and systems to be developed to meet the compliance requirements and to avoid the high costs and disruption associated with unexpected changes close to the compliance date.

By informing APRA of this approach, the ABA is seeking to provide APRA with the opportunity to highlight any concerns ahead of the implementation of APS 222.

I look forward to discussing this approach with APRA on 9 December 2020. Please contact me if you have any further queries concerning APS 222 implementation approach.

Yours faithfully

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ABA approach to APS 222 implementation

1. Step-in risk entities

1.1 Determination of a step-in risk entity

Under of Prudential Standard APS 222 *Associations with Related Entities* (**APS 222**) paragraph 8(h) [1], a **Step-in Risk Entity** is "*an entity to which an ADI is likely to provide support beyond any legal or contractual obligations to do so*". APRA provides a list of indicators ADI's need to consider in evaluating step-in risk in APS 222 paragraph 3 of Attachment B.

The ABA proposes to interpret the Step-in Risk Entity definition and the application of APS 222 Attachment B paragraph 3 in the following way:

- The assessment of a Step-in Risk Entity is a forward-looking point in time estimate
- The step-in risk status of an entity can change over time. An entity that is not a Step-in Risk Entity currently may become a Step-in Risk Entity and vice versa.

1.2 General application of the step-in risk rules

APRA indicated in its Response to Submissions (page 5) that:

> *"Step-in risk describes the possibility that an ADI may step in to support an unrelated entity due to reasons such as reputation or branding, beyond their legal obligation to do so"[2].*

The ABA proposes to interpret the application of the step-in risk rules as applying only to entities that are not related entities under APS 222 (**unrelated entities**). Accordingly, the rules will not typically (see 1.3 below) apply to a subsidiary (including certain "non-consolidated subsidiaries" – defined in Prudential Standard APS 001 *Definitions*[3] (**APS 001**)), associate, substantial shareholder or other type of related entity of an ADI.

The ABA assumes this is because APRA consider that reputation and contagion risk on group members and related entities are already dealt with under Prudential Standard APS 110 *Capital Adequacy* (paragraph 11 – group members) (**APS 110**) [4] and other parts of the revised APS 222 (e.g. provision of support, arm's length dealings, group badging etc for both group members and related entities).

A distinguishing feature of step-in risk is that the support provided by an ADI to an unrelated entity is driven by reputational or branding reasons. Accordingly, where capital or support is provided to an unrelated entity which is driven by commercial or strategic reasons not related to branding or reputational impacts, there will be no step-in risk. Examples of where a step-in risk assessment is not required include (but are not limited to):

- As part of a work-out strategy, an ADI is looking to convert a portion of its debt provided to a borrower to improve the borrower's capital structure and minimise the losses for the ADI.
- An ADI is looking to contribute minority equity into a company to enable the company to fund a project/business strategy that will be of strategic benefit to the ADI.

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[1] APRA *Prudential Standard APS 222 Associations with Related Entities*
[2] APRA 20 August 2019, *Response to Submissions: Revisions to the related entities framework for ADIs*
[3] APRA *Prudential Standard APS 001 Definitions*
[4] APRA *Prudential Standard APS 110 Capital Adequacy*

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1.3 Scope of unrelated entities that require an assessment of step-in risk

The ABA proposes to follow the guidance provided by the October 2017 Basel Committee on Banking Supervision Guidelines: *Identification and Management of Step-in Risk* (**Basel Guidelines**) to identify the types of unrelated entities that will be subject to step-in risk evaluation[5].

These guidelines focus on mitigating potential spill-over effects from the shadow banking system to banks. The Financial Stability Board (**FSB**) describe shadow banking as "*credit intermediation involving entities and activities outside the regular banking system*"[6]. Credit intermediation activities are bank-like activities involving maturity transformation liquidity transformation, leverage, credit risk transfer or similar activities.

Since the focus is on shadow banking activities, the ABA proposes to exclude associations or dealings with unrelated entity banks or insurance companies regulated by APRA or an overseas equivalent, since these are not "shadow" entities[7].

Under the Basel Guidelines where a bank has one or more of the following relationships with an entity[8], an assessment of step-in risk is required:

1) Sponsor – the bank manages or advises the entity, places its securities into the market or provides it with liquidity and/or credit enhancements

2) Debt or equity investor – the bank invests in the entity's debt or equity instruments but excluding:

   a) regular business such as lending relationships to operating entities (e.g. a wholesale loan to a corporate entity); and

   b) investments that arise from market-making (e.g. equity shares held in the trading book or negligible investment); or

3) Other contractual and non-contractual involvement – the bank is exposed to the risks or to equity-like returns from the assets of the entity or related to its performance.

If a step-in risk entity is identified, APRA requires ADI's to specify which of these relationships exist in Reporting Standard *Related entities* 222.2 (see Reporting Form ARF 222.2 *Related entities* (**ARF 222.2**) -1, column 7)[9]. The ABA therefore assumes the above relationships are relevant in determining whether an unrelated entity will be subject to a step-in risk assessment under APS 222.

The ABA interprets the exemption for "lending relationships to operating entities" in 2)a)) above to apply to credit exposures (e.g. loans, commitments, derivatives etc) to corporates (e.g. BHP, Telstra, Rio etc), brokers, securities firms, non-bank finance companies, insurance companies, banks etc since these are all operating entities. Additionally, the ABA considers that the lending relationships to operating entities exemption extends to credit exposures to unrelated third party funds or similar vehicles (**SPV**) (see Appendix A), that are not subject to Prudential Standard APS 120 *Securitisation* (**APS 120 (2018)**)[10], where the only association between an ADI and a SPV is the provision of an arms-length senior debt/credit facility/note to fund the assets of the SPV and not the redemption of investors' securities (e.g. the ADI is not sponsoring or originating assets for the SPV). Where this occurs, the ABA proposes this will not trigger the application of the step-in risk rules.

Given the requirements in APS 120 (2018) for an ADI not to provide implicit support to a securitisation, and APRA's tools in that standard to deal with the provision of implicit support, the ABA considers that the step-in risk rules in APS 222 should not apply to an ADI's relationship with securitisation SPVs, on the basis that APS 120 (2018) already covers the field in this respect.

[5] Basel Committee on Banking Supervision October 2017, *Guidelines: Identification and Management of Step-in Risk*
[6] The Financial Stability Board 18 November 2012, *Global Shadow Banking Monitoring Report*
[7] Consistent with paragraph 25 of the Basel Guidelines
[8] In ARF 222.2-1, if a Step-in risk entity is identified, ADI's need to specify (column 7) which of these relationships exist.
[9] APRA *Reporting Standard Related entities 222.2*
[10] APRA *Prudential Standard APS 120 Securitisation*

The ABA proposes the scope of unrelated entities to be assessed for step-in risk under APS 222 will be limited to:

4) Funds, repackaging vehicles and other like vehicles which are not already captured under APS 120 (2018);

5) Securities firms, brokers or non-bank finance companies granting loans or finance leases, except to the extent these are in respect to non-lending relationships;

6) Funds where the assets under management are not regulatory consolidated with the ADI where a subsidiary of the ADI is the manager and/or where the ADI or a subsidiary of the ADI has a significant influence on the Fund (i.e. treats it as a related entity); and

7) Commercial (non-financial) entities that provide critical operational services (e.g. material business activities in the context of Prudential Standard CPS 231 *Outsourcing* (**CPS 231**)[11]) to the ADI or a subsidiary of the ADI that cannot be replaced in a timely fashion or without excessive cost.

Where an ADI owns a banking or insurance subsidiary (i.e. a related entity) that is regulated by APRA or an overseas equivalent regulator, and that subsidiary has an association with an unrelated entity (but the ADI does not), the ABA proposes to exclude the unrelated entity from the scope of the step-in risk rules in APS 222 on the basis the regulated banking/insurance entity will be adequately capitalised[12], in its own right, to provide support to the unrelated entity.

Appendix B provides some hypothetical examples of where step-in risk will and will not be assessed.

1.4 Process if a step-in risk entity is identified

Where an ADI has identified a Step-in Risk Entity, it must determine (APS 222, paragraph 4 of Attachment A) the materiality of the step-in risk through an assessment of the potential impact on the capital and liquidity of the ADI, if it were to step-in to support the entity.

APRA's APS 220 Appendix A provides that where an ADI has provided a lending facility to an "unrelated third party fund", that is assessed to be a Step-in Risk Entity, the treatment of the loan will be treated as a credit enhancement (i.e. capital deduction or 100 per cent Risk Weighted Assets) not a credit commitment as defined under Prudential Standard APS 113 *Capital Adequacy: Internal Ratings-based Approach to Credit Risk* (**APS 113**)[13]. The ABA assumes this rule applies not just to "loans" but also other credit exposures (e.g. derivatives) to unrelated third-party funds.

APS 222 does not provide guidance on how the capital and liquidity impacts should be assessed in other circumstances (e.g. where an ADI has no exposure to a Step-in Risk Entity or where the ADI has a lending exposure to a non-fund that is a Step-in Risk Entity). Some guidance is provided in:

- The Basel Guidelines (section 4), which present different approaches for assessing the capital and liquidity impacts (e.g. inclusion of the step-in risk entity in the ADI's regulatory scope of consolidation[14] , conversion approach, stress testing, provisioning, inclusion in the liquidity coverage ratio (for other contingent funding obligations that are non-contractual) etc).
- Prudential Standard APS 120 *Funds Management and Securitisation* (**APS 120 (2006)**)[15], which is focussed on ensuring ADI's deal with different risks in funds management activities, including moral risk (which is similar to the concept of step-in risk in APS 222), outlines an approach for funds. In APS 120 (2006)*:"moral risk [is the] possibility an ADI will feel a moral obligation or a commercial need to support a funds management or*

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[11] APRA *Prudential Standard APS 113 Capital Adequacy: Internal Ratings-based Approach to Credit Risk*
[12] The banking or insurance subsidiary may itself be subject to the APS 222 step-in risk rules or equivalent step-in risk rules in its home jurisdiction.
[13] APRA *Prudential Standard APS 113 Capital Adequacy: Internal Ratings-based Approach to Credit Risk*
[14] In Australian terms, the regulatory scope of consolidation is the Level 2 group of an ADI
[15] APRA *Prudential Standard APS 120 Funds Management and Securitisation*

securitisation scheme, or the investors involved in such a scheme, beyond any explicit legal obligation to do so".

Under APS 120 (2006) paragraph 8, if the facilities or services provided by an ADI to the SPV (e.g. a fund) do not meet the criteria in AGN 120.1 to 120.5, the "*ADI may be required to hold capital, on a solo and consolidated group basis, against the full value of the securities issued by the SPV*". This suggests the ADI should estimate the capital assuming (note APS 120 (2006) no longer has any application – see 1.5 below):

a) Regulatory consolidation of the SPV into the ADI's Level 2 group; and

b) The ADI holds all the securities issued by the SPV even if this is not the case (e.g. where the ADI only provides services to the SPV).

The ABA proposes that banks identify all entities that give rise to step-in risk and estimate as appropriate the potential impact on capital and liquidity of a Step-in Risk Entity. ADIs should determine the appropriate choice of measures, based on the nature and extent of the anticipated step-in support in each case.

The type of step-in risk can be broadly categorised as follows:

- Where a Step-in Risk Entity undertakes bank-like activities that would receive an appropriate regulatory treatment under prudential standards (e.g. credit risk RWAs) and where this information is fully available to the ADI; ADIs may decide to consolidate, partially consolidate or apply the conversion approach.
- In other circumstances, such as funds where asset information is not available, critical suppliers, brokers, etc. ADIs should apply the conversion approach as appropriate.

1.5 No further application of Prudential Standard APS 120 *Funds Management and Securitisation* (**APS 120 (2006)**)

APS 120 (2006) aims to ensure ADIs prudently manage risks arising from their involvement in funds management and hold appropriate capital against these risks. This standard could apply to funds that are unrelated entities or related entities.

In the Response to Submissions, APRA states that "*the funds management requirements in APS 120 (2006) will no longer have any application*"[16]. Accordingly, the ABA has interpreted that APS 120 (2006) will no longer apply to funds that are either unrelated entities or related entities. The ABA assumes APRA's rationale for this change is:

- Attachment A of APS 222 will apply to an unrelated entity fund management vehicle that is a Step-in risk entity; and
- Attachment B of APS 222 will apply to a related entity fund management vehicle.

2. Exposures to funding only securitisation, self-securitisation, and covered bond SPVs

The ABA will continue to treat exposures to funding only, self-securitisation as well as to covered bond SPVs (all of which are related entities under APS 222) as exempt under APS 222.

In APS 120, there is no significant credit risk transfer for self-securitisations and funding only securitisations and the assets held by these vehicles will be risk weighted under APS 112 or APS 113. Based on previous guidance provided by APRA to ADIs, under the current APS 222, ADIs have not recognised APS 222 exposures to securitisation vehicles if there is no significant credit risk transfer under APS 120. The ABA proposes to continue with this approach[17] .

[16] APRA 20 August 2019, *Response to Submissions: Revisions to the related entities framework for ADIs* (s 6.1, page 17)
[17] Under paragraph 11 of the revised APS 222 standard, ADI's are required to contact APRA, if they seek to place reliance, for the purposes of complying with the revised APS 222, on a "previous exemption or other exercise of discretion by APRA" under the current APS 222 standard.

The ABA also proposes not to recognise an ADI's exposure to its own covered bond SPV. This is consistent with Prudential Standard APS 121 *Covered bonds* (**APS 121**) paragraph 26 which states that the *"liabilities of the covered bond special purpose vehicle to the ADI and of the issuing ADI to the covered bond special purpose vehicle (and the associated assets) will be disregarded for the purpose of applying Prudential Standards"*[18].

3. Related entities

3.1 Definition of "control"

The definition of "control over an entity" in APS 222 paragraph 8(a) is closely aligned to the accounting standards. The ABA proposes to assume that there will be "control over an entity" if, under the accounting standards:

- The entity is consolidated under AASB 10 *Consolidated Financial Statements*[19]; or
- There is "significant influence" over the entity under AASB 128 *Investments in Associates and Joint Ventures*[20].

3.2 Substantial shareholders

"Substantial shareholders" are entities that have a "substantial holding" greater than 10 per cent under the *Corporations Act 2001*(Cth) s 9. The ABA will proceed on the basis that these holdings:

- are of ordinary voting shares issued by an ADI only. These would exclude, for example, investor holdings of Additional Tier 1 capital (**AT 1**) in an ADI which are not interests in an ADI unless the ADI elects to convert the AT 1 into ordinary voting shares; and
- represent beneficial interests in the shares of an ADI and do not include nominee or trustee holdings where a bare legal interest is held. This is consistent with the *Corporations Act 2001*(Cth) s 609[21].

3.3 Related individuals and relatives

The ABA does not expect exposures to related individuals and relatives will be material. Accordingly, the ABA proposes to leverage off the existing processes for disclosure of related parties under accounting standard AASB 124 *Related Party Disclosures* (**AASB 124**)[22].

The ABA will identify Related Individuals and their relatives as:

- "Key Management Personnel" as defined under AASB 124 paragraph 9; and
- "Close members of the family of a person" as defined under AASB 124 paragraph 9.

Under AASB 124, these parties and an ADI's exposure to them are disclosed annually, in each ADI's end of year financial statement. For ARS 222.0 reporting, where these exposures are expected to be below 0.25 per cent of Tier 1[23] , the ABA proposes to align the frequency of reporting and updating the exposures (i.e. based on the exposures measured in the end of year financial statement) to these parties, to annually, in line with the disclosures made in each ADI's end of year financial statement.

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[18] APRA *Prudential Standard APS 121 Covered bonds*
[19] Australian Accounting Standards Board *AASB 10 Consolidated Financial Statements*
[20] Australian Accounting Standards Board *AASB 128 Investments in Associates and Joint Ventures*
[21] *Corporations Act 2001*(Cth) s 609 outlines the situations that will not give rise to a relevant interest.
[22] Australian Accounting Standards Board *AASB 124 Related Party Disclosures*
[23] This is the same materiality threshold for reporting of exposures to underlying obligors on financial assets held by structured vehicles in the APRA *Prudential Standard APS 221 Large Exposures*.

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4. Related entity funds

4.1 Related entity fund managers

In the Response to APS 222 Submissions (page 17) APRA was asked *"whether the funds management requirements [in Attachment B] apply to a fund manager or strictly to the funds management vehicle or fund"*[24].

APRA's response was *"Attachment B to APS 222 applies to an ADI's associations with a funds management vehicle that is a related entity of the ADI; however, a fund manager may also be subject to the requirements of APS 222 if it is a related entity itself".*

The ABA has interpreted APRA's response as being that where an ADI has a related entity fund manager, the fund manager will not be subject to the APS 222 Attachment B requirements but could be subject to other APS 222 requirements (e.g. provision of support, group badging, arm's length dealings etc).

4.2 APS 222 Attachment B does not apply to unrelated funds management vehicles

APS 222 paragraph 1 of Attachment B states that "[Attachment B] *applies to an ADI's associations with a funds management vehicle that is a related entity of the ADI".* Related entity funds are likely to include funds that the ADI consolidates or has significant influence over [25] which is consistent with APS 222 paragraphs 8(f)(i) and 8(a).

The ABA's interpretation of paragraph 1 is that Attachment B does not apply to a funds management vehicle that is an unrelated entity. Some of the impacts of this interpretation, where an ADI has an association with an unrelated funds management vehicle, are as follows:

- The ADI is not specifically restricted from purchasing more than 20 per cent of the securities issued by the unrelated funds management vehicle
- The ADI may provide a liquidity facility to the unrelated funds management vehicle that could meet the criteria in APS 222 paragraphs 7(a), (b) or (c) but this will not be a CET 1 capital deduction for the ADI
- The ADI may act as an underwriter for the issue of securities issued by the unrelated funds management vehicle and will not be required to deduct the value of the underwriting facility, from the ADI's CET 1, even if the criteria in APS 222 paragraph 8(a), (b) and (c) are met.

Although these (i.e., APS 222 Attachment B) requirements will not apply to an unrelated funds management vehicle, their impacts (e.g., purchasing more than 20 per cent of the securities/providing a liquidity facility that meets APS 222 paragraphs 7(a), (b) or (c)) would need to be assessed under the step-in risk rules.

5. Extended licenced entity (**ELE**) subsidiaries

5.1 APS 222 Attachment C

Where an ADI has obtained APRA approval to treat a subsidiary as an ELE Subsidiary under the current APS 222 standard and an ADI assesses that the subsidiary will continue to be treated as an ELE Subsidiary in the revised APS 222 standard, the ABA will inform APRA of this decision but will proceed on the basis that there is no need to seek re-approval from APRA[26].

[24] APRA 20 August 2019, *Response to Submissions: Revisions to the related entities framework for ADIs* page 17
[25]. Technically, these could also include Funds that are substantial shareholders under paragraph 8(f)(iii)
[26] Under paragraph 11 of the revised APS 222 standard, ADI's are required to contact APRA, if they seek to place reliance, for the purposes of complying with the revised APS 222, on a "previous exemption or other exercise of discretion by APRA" under the current APS 222 standard.

Where an ADI requires transitional relief for a change in status of an ELE Subsidiary, the ADI will enter into bilateral discussions with APRA.

6. APRA reporting

6.1 Reporting Standard ARS 222.0 Exposures to Related Entities (**ARS 222.0**)

For ARS 222.0, the ABA proposes:

- Section A will only report exposures to related entities that are not ELE subsidiaries.
- Section B will report only exposures to ELE Subsidiaries.

For Reporting Form *Related entities* ((**ARF 222.0**), Section B (part 4), the ABA proposes that ADIs will only report on ELE subsidiaries that "*hold or invest in (external) assets*"[27]. For the avoidance of doubt, this means that exposures to related entities and ELE subsidiaries will not be reported here. In addition, Section B (part 4) will also exclude any exposures to ELE Subsidiaries that are set up solely to raise funding on behalf of the ADI.

6.2 Reporting Standard ARS 222.2 Exposures to Related Entities (**ARS 222.2**)

ADI's are required to report total assets of any entities that are identified as a Step-in Risk Entity. On the basis that information on the total assets of a Step-in Risk Entity may not be available at the end of an ADI's financial year, the ABA is proposing to report the total assets based on the latest available information.

6.3 Timeline for reporting

In line with APRA's APS 222 Response to submissions: Revisions to related entities framework for ADIs' Section 6.2[28], the ABA is proposing that APRA allows all advanced/applicant advanced ADIs to submit ARF 222.0 within 30 business days in line with the reporting timeframe under Reporting Form ARF110 Capital Adequacy to facilitate the alignment of reporting of Tier 1 Capital in both the reporting forms. The ABA proposes 35 calendar days for ARS 222.0 reporting consistent with ARF 110. However, the ABA would prefer APRA to allow 40 calendar days to avoid all reporting occurring on the same day.

[27] APRA *Reporting Standard ARS 222.0 Exposures to related entities*
[28] APRA 20 August 2019, *Response to Submissions: Revisions to the related entities framework for ADIs*

Appendix A

Banks received the following email from APRA in February 2020 in respect to lending facilities provided to unrelated third-party funds:

"The capital treatment of a lending facility provided to an unrelated third-party fund may be determined in accordance with APS 112 Capital Adequacy: Standardised Approach to Credit Risk July 2019 (APS 112), or APS 113 Capital Adequacy: Internal Ratings-based Approach to Credit Risk January 2013 (APS 113), similar to any other exposures to unrelated third parties. This is subject to the ADI:

- *satisfying sub-paragraphs 23(a), 23(b), and 23(d) of AGN 120.4*
- *demonstrating that the purpose of the facility is gearing up of investors' interests rather than facilitating redemption of the fund's own securities by reference to investment strategy or mandate of the third-party fund; and*
- *performing an assessment against Attachment A of the draft APS 222 Associations with Related Entities January 2021 (draft APS 222) and satisfying itself that the third-party fund does not present undue step-in risks to it."*

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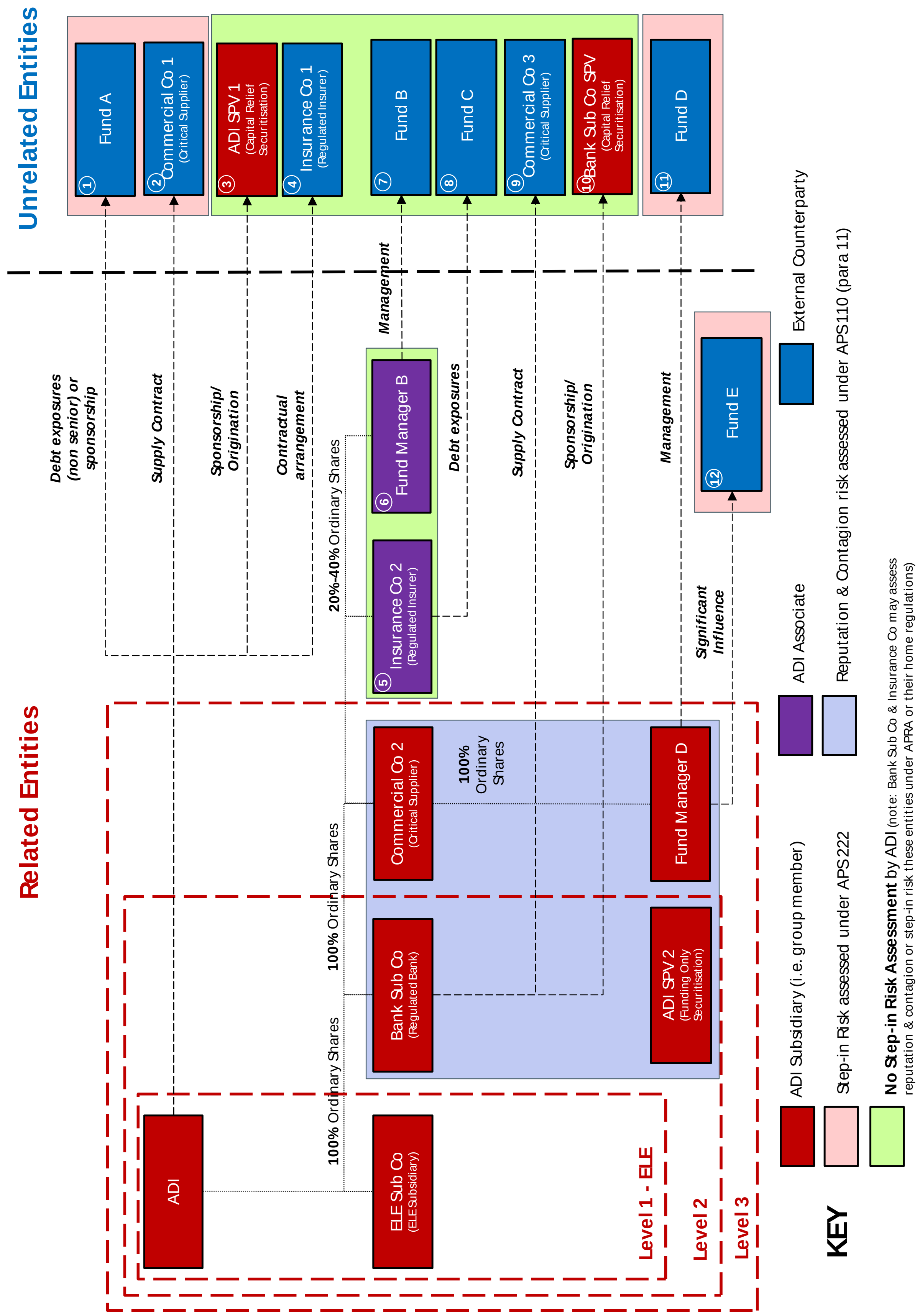
Appendix B



Entity Number	APS 222 Step-in Risk Assessment required?	Rationale
1 & 2	**Yes**	These are Unrelated Entities and the ADI's association with them falls into one or more of sponsorship, debt investor (non-senior) and/or other contractual arrangement.
3	**No**	There is no need to assess step-in risk because the ADI SPV 1 is a capital relief securitisation under APS 120 Securitisation (2018) and therefore implicit support will already be managed and monitored.
4	**No**	Although Insurance Co 1 is an Unrelated entity that the ADI has a contractual arrangement with, it is already subject to specific prudential treatment by APRA or an overseas equivalent regulator (i.e. it is not a "shadow" entity).
5, 6, 7 & 8	**No**	Insurance Co 2[29] and Fund Manager B (Entities 5 & 6) are not Unrelated Entities (since they are associates of the ADI they are Related Entities). Accordingly, a step-in assessment is not required under APS 222[30]. Fund B and Fund C (Entities 7 & 8) are not subject to an APS 222 step-in risk assessment since the ADI has no direct association with them (note: since the ADI has < 50 per cent of the voting rights in Fund Manager B and Insurance Co it is unlikely the ADI will be able to assess the step-in risk Fund Manager B and Insurance Co may have to Fund B and Fund C respectively). Under paragraph 11 of APS 110, Insurance Co 2 and Fund Manager B are not group members (i.e. not subsidiaries) of the ADI and consequently the ADI is not required to assess reputation and contagion risk to these entities.
9 & 10	**No**	Since Bank Sub Co (a Related Entity) is regulated by APRA or an overseas equivalent, the ADI is not required to assess step-in risk on Unrelated Entities (i.e. Commercial Co 3 and Bank Sub Co SPV) that Bank Sub Co may have an association with but which the ADI does not (note: Bank Sub Co is itself required to assess step-in risk on these entities under APS 222 rules if it is regulated by APRA or if its home regulator has equivalent step-in risk rules). Under paragraph 11 of APS 110, the ADI is required to assess its reputation and contagion risk to Bank Sub Co since it is a "group member" of the ADI.
11	**Yes**	Fund D is an unrelated entity and the ADI is sponsoring it indirectly through a non-regulated subsidiary (i.e. Fund Manager D). Since the ADI has 100% of the voting rights in Fund Manager D, an assessment of the step-in risk of Fund D can be made. Under paragraph 11 of APS 110, the ADI is required to assess its reputation and contagion risk to Fund Manager D since it is "group member" of the ADI.
12	**Yes**	Although Fund E is not accounting or regulatory consolidated by the ADI, it is a related entity on the basis Fund Manager D (a subsidiary of the ADI) and/or the ADI has a significant influence on the policies of Fund E. Since the ADI has

[29] Additionally, Insurance Co 2 is already subject to specific prudential treatment by APRA or an overseas equivalent (i.e. is not a "shadow" entity) and so would not be subject to an APS 222 step-in risk assessment on that basis alone.
[30] Note: under the Basel Guidelines, step-in risk would be assessed on Fund Manager B but **not** Insurance Co 2 since Insurance Co 2 is already subject to specific prudential treatment by APRA or an overseas equivalent (i.e. it is not a "shadow" entity).

		100 per cent of the voting rights in Fund Manager D, an assessment of the step-in risk of Fund E can be made.