Australian Banking Association

16 December 2022

General Manager, Policy
Australian Prudential Regulation Authority

By email:

Dear

Modernising the Prudential Architecture

The Australian Banking Association (**ABA**) welcomes the Australian Prudential Regulation Authority's (**APRA**) engagement on and initiatives regarding modernising the prudential architecture (**MPA**). The ABA is very supportive of this multi-year initiative and remains available to assist APRA develop a more interactive, efficient, effective and future proof prudential architecture.

A prudential architecture that is clearer, simpler and more adaptable will benefit all stakeholders. In modernising the prudential architecture, the ABA encourages APRA to also consider ways to:

- Reduce barriers to interacting with and understanding the prudential framework;
- Enhance the usability of the framework; and
- Enhance linkages to APRA's broader work.

The industry has provided initial views on the MPA at the ABA-APRA roundtable on 16 November 2022. Appendix A builds on the roundtable by providing high level feedback to assist APRA develop the future scope and direction of the MPA. The ABA encourages APRA to regularly engage industry as it refines its project plan, to assist banks engage with and provide feedback into this important initiative.

We look forward to continued engagement on the MPA, including deeper analysis of the opportunities it provides for both APRA and industry, as well as other stakeholders and industry observers.

If you require further information or would like to discuss any of the content of this letter further, please do not hesitate to contact me on

Regards,

Policy Director
Australian Banking Association

About the ABA

The Australian Banking Association advocates for a strong, competitive and innovative banking industry that delivers excellent and equitable outcomes for customers. We promote and encourage policies that improve banking services for all Australians, through advocacy, research, policy expertise and thought leadership.

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Appendix A: Initial industry views on modernising the prudential architecture

Reducing barriers to interacting with and understanding the prudential framework

Reducing multiple sources of truth

When engaging with APRA's prudential system, entities need to consider requirements and views from multiple APRA sources. These include banking and cross-industry standards, banking and cross-industry guides, FAQs, letters, industry roundtables/workshops and bilateral meetings. There is scope to consolidate these 'sources of truth' and to improve the way in which they are interlinked, including driving greater consistency between prudential standards. APRA's 'combined' CPS 190 and CPG 190 is a positive move in this direction. The ABA encourages APRA to further develop interlinkages, including exploring more digital solutions.

In consolidating the various 'sources of truth', it is important to ensure that the relevant history and previous guidance is not lost, for example through the development of an archive of historical versions and previous guidance. It will also be important to balance the efficiency of a more singular 'source of truth' against the flexibility and timeliness of providing prompt updated feedback, for example, via FAQs and letters.

Improving digitalisation

A lack of digitalisation of the prudential framework currently inhibits the ability of banks' systems to interact with the framework. There is a need for APRA to work closely with banks (and AI/regtech providers) to develop a framework that can most optimally interact with banks' systems, such as credit approval, compliance and assurance systems, (now and in the future) and allow them to leverage technological solutions.

In tandem, there is a need for clearer guidance on APRA's appetite for banks utilising technological solutions (without breaching prudential requirements).

The ABA notes the recent release of the new *Guide for Authorised Deposit-taking Institution Boards* and the accompanying spreadsheet of requirements. This is a positive initiative which consolidates Boards' requirements, reduces uncertainty and allows greater take up of technological solutions. One of the key practical challenges for ADIs (and auditors) in managing compliance with prudential obligations is the ability to consolidate obligations across all the standards and produce a 'role-based' or 'activity-based' profile of obligations. Consolidated documents will help drive more consistent awareness and understanding, and better compliance with the obligations.

Enhancing the usability of the framework

Increase navigability and searchability

The usability of the prudential framework would be enhanced if it were move easily navigated and searchable. As noted above, it would be valuable, to industry and observers, to be able to produce a document (or a digital view) that consolidates all the individual requirements across each of the relevant standards based on a particular theme or business activity.

It is currently difficult to navigate across the various standards that relate to the same subject, for example, in the capital framework, it is difficult to navigate across APS 110 Capital Adequacy, APS 111 Capital Adequacy: Measurement of Capital, APS 112 Capital Adequacy: Standardised Approach to Credit Risk and APS 113 Capital Adequacy: Internal Ratings-based Approach to Credit Risk. It is also very difficult to search the framework by a specific topic, for example requirements related to valuations. Developing a standard taxonomy may also enhance searchability.

Simplification of requirements and reduction of duplication:

The ABA is supportive of APRA's efforts to reduce duplication of prudential requirements, such as the development of CPS 230 Operational Risk Management to replace CPS 231 Outsourcing and CPS 232

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Business Continuity Management. The ABA notes there will be a need to balance simplification with providing sufficient detail to understand APRA's intent. Close engagement with industry during the development phase of consolidated/simplified standards will be essential for optimising outcomes.

There is also an opportunity to reduce duplication of definitions and terminology across standards, for example, considering 'senior manager' in CPS 511 Remuneration and CPS 520 Fit and Proper. This should be coupled with better leveraging current requirements and definitions when developing new standards, rather than reproducing those requirements and definitions.

International harmonisation and substituted compliance:

Institutions with operations in foreign jurisdictions must comply with varying regulatory and legislative requirements. There is an opportunity for APRA's regulatory framework to better align to, or accept through substituted compliance, the requirements in foreign jurisdictions. A greater allowance for 'group approaches' to regulatory compliance would also reduce complexity and regulatory burden.

New risks, new rules

Further detail regarding the "new risks, new rules" component of the MPA information paper would be welcomed by industry. At the appropriate time, the ABA and industry look forward to engaging on this aspect of the MPA, including at a more technical level.

Some topics that could be considered in this area include:

- Industry Third Party Concentration Risk;
- More sophisticated systemic risk monitoring;
- Collaborative cyber defence; and
- Nature-related risks (for example, expanding on CPG 229 Climate Change Financial Risks to incorporate risks of this class).

Enhancing linkages to APRA's broader work.

The MPA should also consider how the framework does and could link to APRA's broader work.

Linkages to the Financial Accountability Regime (FAR)

Clearer linkages between the prudential framework and FAR would likely increase the consistency of industry's approach and create efficiencies.

Data and report

While data collection and reporting forms are outside the scope of the MPA, and being considered in APRA's strategic initiative, *Enabling better data-driven decisions*, there is the opportunity to consider the interlinkages between the prudential and reporting frameworks. Changes and definitions in the prudential framework can have a material impact on data and reporting requirements. Making the linkages between these frameworks closer, more traceable and transparent would reduce regulatory burden while driving more consistent approaches across the industry.