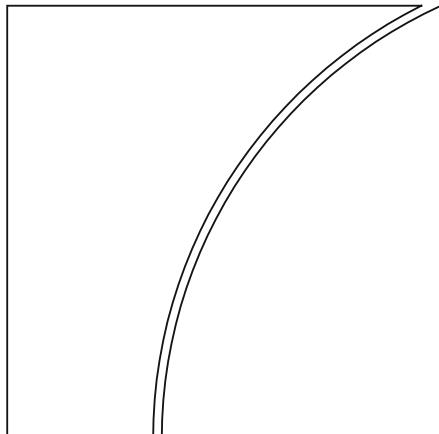


# Basel Committee on Banking Supervision



## Regulatory Consistency Assessment Programme (RCAP)

### Assessment of Basel NSFR regulations – Australia

July 2019



BANK FOR INTERNATIONAL SETTLEMENTS

**Note that this report refers to the RCAP grades prior to October 2025. The grade 'materially non-compliant (MNC)', ie one notch above the lowest grade, has since been renamed to 'partially non-compliant (PNC)' for greater clarity**

This publication is available on the BIS website ([www.bis.org](http://www.bis.org)).

© *Bank for International Settlements 2019. All rights reserved. Brief excerpts may be reproduced or translated provided the source is stated.*

ISBN 978-92-9259-284-4 (online)

## Contents

Glossary.....	1
Preface .....	2
Executive summary.....	3
Response from the Australian Prudential Regulation Authority .....	4
1 Assessment context.....	5
1.1 Status of NSFR implementation.....	5
1.2 Regulatory system .....	5
1.3 Structure of the banking sector .....	6
1.4 Scope of the assessment .....	6
2 Assessment findings .....	7
2.1 Assessment grades and summary of findings.....	7
2.2 Detailed assessment findings.....	8
2.3 Observations on the NSFR implementation in Australia.....	10
Annexes.....	11
Annex 1: RCAP Assessment Team and Review Team .....	11
Annex 2: List of Basel standards and implementing regulations issued by APRA .....	12
Annex 3: Key liquidity indicators of the Australian banking system.....	13
Annex 4: Materiality assessment .....	14
Annex 5: Areas where APRA's rules are stricter than the Basel standards .....	15
Annex 6: Elements of the NSFR subject to national discretion.....	16
Annex 7: RCAP-LCR follow-up: host jurisdiction securities in HQLA.....	18



## Glossary

ADI	Authorised Deposit-Taking Institution
APG	ADI Prudential Practice Guide
APS	ADI Prudential Standard
ARS	ADI Reporting Standard
APRA	Australian Prudential Regulation Authority
BIS	Bank for International Settlements
C	Compliant (grade)
G-SIB	Global systemically important bank
HQLA	High-quality liquid assets
LC	Largely compliant (grade)
LCR	Liquidity Coverage Ratio
MNC	Materially non-compliant (grade)
NC	Non-compliant (grade)
NSFR	Net Stable Funding Ratio
RCAP	Regulatory Consistency Assessment Programme
SIG	Supervision and Implementation Group

## Preface

The Basel Committee on Banking Supervision (Basel Committee) places a high priority on the implementation of regulatory standards underpinning the Basel III framework. The prudential benefits from adopting Basel standards can only fully accrue if these are implemented fully, consistently and in a timely manner by all member jurisdictions. The Committee established the Regulatory Consistency Assessment Programme (RCAP) to monitor, assess and evaluate its members' implementation of the Basel framework.

This report presents the findings of an RCAP Assessment Team on the domestic adoption of the Basel Net Stable Funding Ratio (NSFR) standard in Australia. The assessment focused on the completeness and consistency of the domestic regulations in force on 31 March 2019, as applied to locally incorporated Authorised Deposit-taking Institutions (ADIs) in Australia, with the Basel NSFR standard. Issues related to prudential outcomes, the adequacy of liquidity, the resilience of the banking system or the supervisory effectiveness of the Australian authorities were not in the scope of this assessment. The assessment relied on regulations and other information and explanations provided by the Australian authorities and ultimately reflects the view of the Basel Committee.

The RCAP Assessment Team was led by Arthur Yuen, Deputy Chief Executive, Hong Kong Monetary Authority. The team comprised four technical experts from Georgia, Japan, the Philippines, and the United States (see Annex 1). The main counterpart for the assessment was the Australian Prudential Regulation Authority (APRA). The work was coordinated by the Basel Committee Secretariat with support from staff from the Team Leader's organisation.

The assessment began in October 2018 and comprised three phases: (i) self-assessment by the assessed jurisdiction's authorities; (ii) an assessment phase (November 2018 to March 2019), including an on-site assessment involving discussions with the Australian authorities and other stakeholders; and (iii) a review phase (April 2019 to May 2019), including a technical review of the Assessment Team's findings by a separate RCAP Review Team, the Committee's Supervision and Implementation Group, the RCAP Peer Review Board and the Basel Committee. More information on the RCAP assessment process is available on the Committee's website.<sup>1</sup>

The RCAP Assessment Team acknowledges the professional cooperation received from APRA counterparts throughout the assessment process. In particular, the team sincerely thanks the staff at APRA for playing an instrumental role in coordinating the assessment process.

<sup>1</sup> See [www.bis.org/bcbs/implementation.htm](http://www.bis.org/bcbs/implementation.htm).

## Executive summary

The Australian framework for NSFR requirements was finalised in December 2016 through the publication of the final revised Prudential Standard APS 210 Liquidity (APS210) and Prudential Practice Guide APG 210 Liquidity. The NSFR requirements came into effect on 1 January 2018. The associated reporting framework, as set out in the revised Prudential Standard APS 330 Public Disclosure, was finalised in April 2018 and came into effect on 1 July 2018. The NSFR requirements in Prudential Standard APS 210 Liquidity apply to locally incorporated Authorised Deposit-taking Institutions (ADIs) in Australia which are also subject to the LCR (ie branches of foreign banks are not subject to the NSFR). Currently, 14 ADIs are subject to the NSFR and one ADI is scheduled to be subject to the NSFR on 1 January 2020. The ADIs subject to the NSFR include some smaller ADIs in addition to the large internationally active ADIs.

Overall, as of 31 March 2019, the NSFR regulations in Australia are assessed as compliant with the Basel NSFR standards. This is the highest of the four possible grades. The components of the NSFR – (i) scope, minimum requirement and application issues; (ii) available stable funding; (iii) required stable funding; and (iv) disclosure requirements – are also assessed as compliant. Overall, there were two non-material findings, one in the available stable funding component and one in the disclosure requirements component. In addition two observations related to the required stable funding component and one to the disclosure requirements. The Assessment Team compliments APRA for their implementation of, and alignment with, the Basel NSFR framework.

In addition to the formal assessment of the NSFR standard and disclosure requirements, this report contains an annex with a follow-up to an issue raised in the RCAP of the Australian LCR framework regarding HQLA in a host jurisdiction. The annex reviews the implementation of the BCBS internal guidance that limits the inclusion of host jurisdiction securities in HQLA to the stressed net cash outflows denominated in the local currency of that jurisdiction.

## Response from the Australian Prudential Regulation Authority

APRA wishes to acknowledge the open and professional manner with which the RCAP team conducted the assessment and to express our sincere thanks to Mr Arthur Yuen and the team. As with the LCR RCAP, the NSFR RCAP process provided a valuable opportunity to reflect on APRA's implementation of the NSFR, benchmark APRA's rules against our global peers and identify areas for improvement.

We welcome the overall rating of "compliant" with the Basel NSFR standards. As noted in the report, the Australian implementation of the NSFR is consistent with the Basel standard, with two non-material deviations being identified. In implementing the NSFR, APRA has taken a pragmatic approach to a small number of jurisdiction-specific circumstances not strictly contemplated by the Basel standard. However, at all times, the intent has been to align with the spirit of the Basel standard. We appreciate the effort made by the RCAP team to understand APRA's approach.

Together with the LCR, the implementation of the NSFR has improved the liquidity risk management of our largest and most complex ADIs. APRA will continue to focus on the effective operation of the NSFR through rigorous routine supervision.

## 1 Assessment context

### 1.1 Status of NSFR implementation

APRA, the prudential regulator of the financial services sector in Australia, published Prudential Standard APS 210 Liquidity and the associated reporting framework that gave effect to major elements of the Basel III liquidity reforms in Australia. APS 210 provides for the introduction in Australia of the LCR and NSFR. The NSFR requirements of APS 210 came into effect on 1 January 2018, while the NSFR disclosure requirements came into effect on 1 July 2018.

APRA's Prudential Standards apply to all ADIs in Australia, including small and medium-sized commercial banking institutions that are not internationally active, although they apply to the smallest domestic institutions with proportionality to take into account the size and nature of their activities. All ADIs are subject to APS 210 which includes quantitative and qualitative criteria consistent with the Basel Sound Principles and Basel III liquidity framework. APRA determines which ADIs are subject to the LCR (typically larger and more complex firms with higher inherent liquidity risks). All locally incorporated ADIs that are subject to the LCR are also subject to the NSFR (ie branches of foreign banks are not subject to the NSFR). Currently, 14 ADIs are subject to the NSFR and one ADI is scheduled to be subject to the NSFR on 1 January 2020.

### 1.2 Regulatory system

Australia has a functional model of financial supervision in which the prudential oversight of all ADIs, insurers and superannuation funds (other than self-managed funds) rests with APRA. The Australian Securities and Investments Commission (ASIC) is responsible for market and corporate conduct, including consumer protection. The Reserve Bank of Australia has responsibility for overseeing financial system stability and the payments system. Coordination takes place through the Council of Financial Regulators (CFR).

APRA was established under the Australian Prudential Regulation Authority Act 1998 on 1 July 1998 and is responsible for authorising and supervising ADIs. APRA is solely responsible for implementing Basel III in Australia. It derives its legal authority to formulate and amend Prudential Standards from the Banking Act (1959) (Banking Act). APRA's core mission is "to establish and enforce prudential standards and practices designed to ensure that, under all reasonable circumstances, financial promises made by the institutions APRA supervises are met within a stable, efficient and competitive financial system". APRA has statutory powers to regulate and intervene in the operations of ADIs, including the power to revoke a supervised entity's authorisation if it fails to meet statutory requirements or prudential standards; make, apply and enforce prudential standards; collect information, conduct onsite examinations and require third-party audits; and act in certain circumstances to protect depositors and to maintain the stability of the financial system by investigating, giving directions and assuming control of ADIs in difficulty. APRA can appoint a statutory manager to assume full control of the ADI. APRA has developed a regulatory framework for ADIs and non-operating holding companies (NOHCs) based on the banking supervision principles published by the Basel Committee. APRA also acts under the Financial Sector (Collection of Data) Act 2001 as the national statistical agency for the financial sector. ADIs must provide financial data in regular standardised reports to APRA.

Australia has implemented an Alternative Liquidity Approach (ALA) as provided for by the Basel LCR standard for use in jurisdictions where there is an insufficient supply of HQLA in the domestic currency. The Australian ALA consists of a committed liquidity facility (CLF) provided by the Reserve Bank of Australia (RBA) to ADIs requiring additional HQLA with a certain level of fee charge. The CLF is intended to be sufficient in size to compensate for the lack of sufficient HQLA (mainly Australian government and semi-

government securities) in Australia for ADIs to meet their LCR requirements. CLF collateral consists of RBA repo-eligible third party debt securities and self-securitised assets.

The treatment of CLF eligible securities follows from the Basel NSFR standard utilisation of LCR HQLA definitions. As specified in the Basel NSFR standard, The HQLA in the NSFR is the same HQLA that is defined in the LCR, which does not include operational requirements. APRA treats CLF eligible collateral as Level 1 HQLA up to the amount of the RBA's CLF commitments offered to individual ADIs, while the portion of CLF collateral exceeding the commitment limit is not treated as HQLA.<sup>2</sup> The RSF factor assigned to the CLF eligible collateral is applied to the carrying value (ie pre-haircut) of the securities as is done with all other balance sheet assets in the NSFR.

However, only loans to financial institutions secured by Level 1 HQLA excluding CLF eligible collateral where the ADI can freely rehypothecate the received collateral are assigned a 10% RSF factor. Loans secured by CLF eligible collateral, Level 2 HQLA or non-HQLA are assigned a 15% RSF factor.

### 1.3 Structure of the banking sector

The Australian banking sector is dominated by four major banks that provide a full range of institutional, commercial and retail banking services: Australia and New Zealand Banking Group Limited, Commonwealth Bank of Australia, National Australia Bank Limited, and Westpac Banking Corporation. Several smaller banks, building societies and credit unions operate in particular sectors or regions.

APRA has determined that the "big four" banks (see above) are domestic systemically important banks (D-SIBs). None of the Australian incorporated banks meet the criteria for classification as a global systemically important bank (GSIB). These four banks as well as Macquarie Bank are considered to be internationally active. There is no state-owned bank in Australia. In evaluating the materiality of its findings, the RCAP Assessment Team focused on the five largest banks in Australia. Together, these banks account for about 80% of the banking sector's total assets. Annex 3 provides further information on the banking system in Australia and the NSFR of these sample banks.

### 1.4 Scope of the assessment

The Assessment Team considered the NSFR requirements applicable to internationally active banks in Australia as of 31 March 2019. The assessment had two dimensions:

- A comparison of domestic regulations with the Basel NSFR standard to ascertain that all the required provisions have been adopted (*completeness* of the regulations); and
- Whether there are any differences in substance between the domestic regulations and the Basel NSFR standard and, if so, their significance (*consistency* of the regulations).

In its assessment, the RCAP Assessment Team considered all binding documents that effectively implement the Basel NSFR standard in Australia. Annex 2 lists the Basel standards used as the basis for the assessment. The assessment did not evaluate the adequacy of liquidity or the resilience of the banking system in Australia or the supervisory effectiveness of APRA.

As set out in the RCAP methodology, the Assessment Team evaluated the materiality and potential materiality of identified deviations between the Basel NSFR standard and the local regulations. The quantification was limited to a sample of banks. In addition, the Assessment Team reviewed the non-quantifiable aspects of identified deviations and applied expert judgment as to whether the domestic

<sup>2</sup> This was discussed in the assessment of the Australian implementation of the LCR, notably in the context of inflow rates applicable to other contractual cash flows. See the Australian RCAP-LCR report for more details, available at [www.bis.org/bcbs/publ/d419.pdf](http://www.bis.org/bcbs/publ/d419.pdf).

regulations meet the Basel framework in letter and in spirit. The materiality analysis is summarised in Annex 4, which also lists the sample of banks.

The Assessment Team noted that, in some areas, the assessed jurisdiction's rules go beyond the minimum Basel standards. Although these elements (listed in Annex 8) provide for a more rigorous implementation of the Basel framework, they have not been taken into account for the assessment of compliance.

The outcome of the assessment is summarised using a four-grade scale, at the level of both each of the four key components of the Basel NSFR framework and the overall assessment of compliance. The four grades are compliant, largely compliant, materially non-compliant and non-compliant.

## 2 Assessment findings

### 2.1 Assessment grades and summary of findings

Overall, the Assessment Team finds the implementation of the NSFR in Australia to be compliant with the Basel standards. This grade is based on the materiality assessment (summarised in Annex 4).

Assessment grades

Table 1

Component of the Basel NSFR framework	Grade
Overall grade	C
Scope, minimum requirement and application issues	C
Available stable funding (numerator)	C
Required stable funding (denominator)	C
NSFR disclosure requirements	C

Assessment scale: C (compliant), LC (largely compliant), MNC (materially non-compliant) and NC (non-compliant).

#### 2.1.1 Scope, minimum requirement and application issues

The principles regarding the scope, minimum requirement and application issues under the Australian NSFR standard are assessed as compliant with the Basel requirement. The Assessment Team does not have any particular finding in this component.

#### 2.1.2 Required stable funding

The Australian implementation of the required stable funding component is assessed as compliant with the Basel standards. The Assessment Team does not have findings in this component. There were two observations with regard to required stable funding, one of them relating to the limitation on the RSF factors for assets encumbered for exceptional central bank liquidity operations. The Australian regulation does not explicitly contain the requirement that assets encumbered for exceptional central bank liquidity operations must not receive an RSF factor lower than that for the same class of assets without encumbrance. While not containing an explicit limit, APRA requires approval before an ADI can use a lower RSF factor as part of its exercise of national discretion. Further, APRA stated that they would have no reasonable basis to assign a lower RSF factor for encumbered assets and it would not be logical for a regulatory authority to do so. Given the stated intention of APRA and the fact that there have never been any exceptional central bank liquidity operations, this is noted as an observation.

The second observation relates to open (non-maturity) reverse repo transactions. Under the Basel NSFR standard and FAQ 7, a non-maturity reverse repo should be assigned an RSF of 100% (to continue over the one-year term) unless banks can demonstrate to supervisors that the non-maturity reverse repo would effectively mature in a different period. APRA allows ADIs with non-maturity reverse repos that are managed on a daily basis and can be unwound at short notice by either party to assign a lower RSF based on a maturity of less than six months. This approach aligns with FAQ 7, which allows a different RSF factor when supervisors are convinced that a non-maturity reverse repo would mature in a different period, which in the case of APRA uses an RSF factor assigned to less than six months. Based on actual industry practice, the vast majority of repos are unwound within six months. However, for those repos that are not unwound within six months a higher RSF should be assigned. Since only a small amount have not been unwound within six months, and this appears to be due to operational oversight, this is noted as an observation.

### 2.1.3 Available stable funding

The Australian implementation of available stable funding is assessed as compliant with the Basel standard with one non-material deviation. The deviation relates to the treatment of certain intermediated deposits as retail.<sup>3</sup> In the NSFR, retail deposits are regarded as more stable and are thus assigned higher ASF factors than deposits from financial or corporate entities. APRA allows for some intermediated deposits that satisfy strict look-through criteria to be assigned an ASF factor as if such deposits were retail deposits despite the presence of a third-party intermediary. The look-through criteria are not explicitly set out in the Basel NSFR standard, which does not take into account the unique treatment of intermediated deposits in Australia. However, the look-through criteria required by APRA for an ADI to classify these deposits as retail deposits ensure that only those deposits that behave as retail are assigned the preferential ASF factor for retail deposits. The intermediated deposits included as retail deposits are consistent with the intent of the Basel NSFR standard retail ASF treatment. Since the APRA intermediated deposit treatment limits the application of the preferential ASF factor to only those deposits that behave similarly to retail deposits, this finding is therefore considered a non-material deviation from the Basel NSFR standard.

### 2.1.4 Disclosure requirements

The Australian implementation of the disclosure standards is assessed as compliant with the Basel standard with one non-material deviation, which relates to the Australian regulations not explicitly subjecting internationally active banks to semi-annual NSFR disclosures. Since all internationally active banks in Australia are currently subject to semi-annual NSFR disclosures, this finding is considered a non-material deviation from the Basel NSFR standard.

## 2.2 Detailed assessment findings

### 2.2.1 Available stable funding

Section grade	Compliant
Basel paragraph number	22–24: Intermediated Deposits
Reference in the domestic regulation	APS 210, Attachment C paragraphs 12–14
Finding	Basel standards under paragraphs 22 and 23 set out the NSFR treatment of retail deposits. These types of deposit are regarded as more stable and thus carry a higher ASF factor than deposits from financial institutions or corporates.

<sup>3</sup> This was discussed in the assessment of the Australian implementation of the LCR. The Assessment Team opined that the treatment applied to such deposits in Australia is aligned in substance with the intent of the Basel LCR standard; however, the Team acknowledged that, in form, this is still a deviation. See the Australian RCAP-LCR report for more details, [www.bis.org/bcbs/publ/d419.pdf](http://www.bis.org/bcbs/publ/d419.pdf).

	<p>Intermediated deposits are deposits placed by a person with an intermediary, which then places these funds with an ADI. Basically, intermediaries are considered as financial institutions, which include superannuation funds and providers of investment platforms. However, APRA recognises these deposits as retail subject to certain conditions. Based on APRA rules, an ADI can classify intermediated deposits as retail deposits when these comply with all the look-through criteria provided under paragraph 35 of Attachment A, APS 210.</p> <p>APRA stated that there is no contractual maturity for the relationship between an ADI and an intermediary. An ADI may maintain a relationship with an intermediary continuously unless an intermediary gives a notice of termination to an ADI in advance of six or 12 months. A minimum 12-month notice period requirement is one of the conditions for qualifying the intermediated deposits under a 95% or 90% ASF factor, while a minimum six-month notice period requirement would only cause the intermediated deposits to be assigned a 50% ASF factor. A notice period of less than six months will have a 0% ASF factor.</p> <p>The Assessment Team assesses this finding as non-material. The look-through approach is not set out in the Basel NSFR standard but the look-through criteria set by APRA ensure that the depositor ultimately retains control over the deposits. In this case, the intermediary simply acts as a pass-through and cannot make investment decisions on behalf of the person regarding deposits or withdrawals. Failure to comply with these conditions would render the deposits as coming from a financial institution that attracts lower ASF factors.</p> <p>Meanwhile, the notice period requirement has no impact on the behaviour of the depositor as represented by APRA. Since this is an agreement between the ADI and the intermediary, this only serves as an additional assurance that the intermediary cannot unilaterally withdraw the funds.</p> <p>Data showed that as at December 2018 three sample banks reported placements considered as intermediated deposits and classified under the "less stable" category. This basically points to member-directed superannuation deposits or SMSFs, which are classified as "less stable". Meanwhile, all five sample banks reported nil amounts for intermediated deposits that qualify as "stable".</p>
Materiality	Not material

## 2.2.2 Disclosure requirements

<b>Section grade</b>	<b>Compliant</b>
Basel paragraph number	LIQ2, Frequency
Reference in the domestic regulation	Prudential Standard APS 330 Public Disclosure paragraph 42 and Corporations Act 2001
Finding	<p>The Basel standard requires all internationally active banks at the top consolidated level to publish their NSFR disclosures semi-annually. However, under APRA regulation, disclosure is at the same frequency and concurrent with the lodgement of an ADI's financial reports under the Corporations Act. Under the Corporations Act, not all ADIs file financial reports at least semi-annually.</p> <p>According to data supplied by APRA, there are six small ADIs that file annual financial reports and therefore file NSFR disclosure reports only annually. The six ADIs that file annually accounted for 3.7% of total NSFR ADI assets as of 30 September 2018. The other eight ADIs, including the large internationally active ADIs, account for 96.3% of NSFR ADI assets, and file NSFR disclosure reports semi-annually. Since the internationally active ADIs file NSFR disclosure reports semi-annually, the deviation is not material.</p>
Materiality	Not material

## 2.3 Observations on the NSFR implementation in Australia

The following observations highlight certain special features of the regulatory implementation of the Basel NSFR standards in Australia. These are presented to provide additional context and information. Observations are considered compliant with the Basel standards and do not have a bearing on the assessment outcome.

### 2.3.1 Required Stable Funding

Basel paragraph number	31: Assets encumbered for exceptional central bank liquidity operations
Reference in the domestic regulation	APS 210, Attachment C paragraph 24
Observation	The Basel standard provides that, for the purposes of calculating the NSFR, assets that are encumbered for exceptional central bank liquidity operations may receive a reduced RSF factor, which must not be lower than the RSF factor applied to the equivalent asset that is unencumbered. APRA does not include the limitation that the RSF should not be lower than the equivalent unencumbered asset. This could open an interpretation of assigning a lower RSF factor compared with an equivalent unencumbered asset. APRA stated that it has not encountered any assets encumbered for exceptional central bank liquidity operations and that, if such a scenario were to arise, APRA would have no reasonable basis on which to assign an RSF factor lower than the RSF factor applied to the equivalent asset that is unencumbered.
Basel paragraph number	29: Open reverse repo
Reference in the domestic regulation	APS 210, Attachment C paragraph 37 and footnote 28
Observation	The Basel standard provides that assets should be allocated to the appropriate RSF factor based on their residual maturity. This has implications for an open reverse repo or a non-maturity reverse repo which under the NSFR FAQ has been clarified. NSFR FAQ 7 provides that a non-maturity reverse repo should be assigned an RSF of 100% (to continue over the one-year term), unless banks can demonstrate that the non-maturity reverse repo would effectively mature in a different period. APRA stated that ADIs with non-maturity reverse repos that are managed on a daily basis, and can be unwound at short notice by either party, are allowed to assign a lower RSF based on a maturity of less than six months to such reverse repos. This should be set out in the relevant ADI's policies and procedures. Further, based on industry practice, most repos are unwound within six months. Given this, non-maturity reverse repos can be allocated to the less than six months maturity bucket.

### 2.3.2 Disclosure requirements

Basel paragraph number	BCBS 324, paragraph 8: Implementation Date
Reference in the domestic regulation	APS 330 Public Disclosure
Observation	APRA prudential standard APS 330 Public Disclosure commenced on 1 July 2018 rather than 1 January 2018, as Basel requires. Under APRA regulation, ADIs reported NSFR only once during 2018 instead of twice as required under the Basel standard. As this is not an ongoing issue, it is noted as an observation.

## Annexes

### Annex 1: RCAP Assessment Team and Review Team

#### Assessment Team Leader

Mr Arthur Yuen Hong Kong Monetary Authority

#### Assessment Team members

Mr Alvin Gamat	Bangko Sentral ng Pilipinas
Mr James Weinberger	US Office of the Comptroller of the Currency
Ms Teona Kontridze	National Bank of Georgia
Ms Rie Asakura	Japan Financial Services Agency

#### Supporting members

Mr Marcel Bluhm	Hong Kong Monetary Authority
Mr Thomas Wong	Hong Kong Monetary Authority
Mr Mark Pocock	Basel Committee Secretariat
Mr Olivier Prato	Basel Committee Secretariat

#### Review Team members

Mr Toshio Tsuiki	Basel Committee Secretariat
Mr Simon Dixon	Bank of England, Prudential Regulatory Authority
Ms Anne Lécuyer	European Central Bank, Single Supervisory Mechanism
Mr Tuang Lee Lim	Monetary Authority of Singapore

## Annex 2: List of Basel standards and implementing regulations issued by APRA

The following Basel standards were used as the basis of this RCAP assessment:

- *Basel III: the Net Stable Funding Ratio*, October 2014
- *Pillar 3 disclosure requirements – consolidated and enhanced framework*, March 2017
- *Implementation of Net Stable Funding Ratio and treatment of derivative liabilities*, October 2017
- *Basel III: The Net Stable Funding Ratio – Frequently Asked Questions*, February 2017

Table A.1 lists the regulations issued by APRA to implement the NSFR in Australia. Previous RCAP assessments of APRA's implementation of the Basel standards considered the binding nature of regulatory documents in Australia.<sup>4</sup> This RCAP Assessment Team did not repeat that assessment, but instead relied on the previous assessments' findings. Those assessments concluded that the types of instrument described in Table A.1 could be considered as binding on banks and supervisors for the purposes of an RCAP assessment.

Overview of relevant APRA liquidity regulations

Table A.1

Domestic regulations	Type, version and date
APS 210 Liquidity	Prudential Standard APS 210 Liquidity (January 2018) <a href="http://www.legislation.gov.au/Details/F2017L00047/c527fa49-8e9f-4ca3-bb0b-078884641c15">www.legislation.gov.au/Details/F2017L00047/c527fa49-8e9f-4ca3-bb0b-078884641c15</a>  Prudential Practice Guide APG 210 Liquidity (December 2016) <a href="http://www.apra.gov.au/sites/default/files/161123-APG-210.pdf">www.apra.gov.au/sites/default/files/161123-APG-210.pdf</a>  Liquidity Frequently Asked Questions (April 2018) <a href="http://www.apra.gov.au/frequently-asked-questions-faqs-liquidity">www.apra.gov.au/frequently-asked-questions-faqs-liquidity</a>
APS 330 Public Disclosure	Prudential Standard APS 330 Public Disclosure (July 2018) <a href="http://www.legislation.gov.au/Details/F2018L00509/76f915a7-2663-4048-9da3-b0cb84b1b5b4">www.legislation.gov.au/Details/F2018L00509/76f915a7-2663-4048-9da3-b0cb84b1b5b4</a>
ARS 210 Reporting	Reporting Standard ARS 210.0 Liquidity (January 2018) <a href="http://www.legislation.gov.au/Details/F2017L01390/095affe4-49fc-4017-adb9-065aee8dc982">www.legislation.gov.au/Details/F2017L01390/095affe4-49fc-4017-adb9-065aee8dc982</a>

Source: APRA.

<sup>4</sup> See Annex 5 of the BCBS RCAP-LCR report for Australia, [www.bis.org/bcbs/publ/d419.pdf](http://www.bis.org/bcbs/publ/d419.pdf).

## Annex 3: Key liquidity indicators of the Australian banking system

Overview of Australian banking sector liquidity as of 31 December 2018

Table A.2

Size of banking sector (AUD millions)		
Total exposures of all banks operating in Australia (including off-balance sheet exposures) <sup>1</sup>		5,072,703
Total assets of all locally incorporated internationally active banks		3,850,652
Total assets of locally incorporated banks to which liquidity standards under the Basel framework are applied		4,215,200
Number of banks		
Number of banks operating in Australia (excluding local representative offices)		144
Number of global systemically important banks (G-SIBs)		0
Number of D-SIBs		4
Number of banks which are internationally active		5
Number of banks required to implement Basel III liquidity standards		15
Number of banks required to implement domestic liquidity standards <sup>2</sup>		129
Breakdown of NSFR for 5 RCAP sample banks (AUD, millions)		Unweighted
Capital		321,894
Stable deposits from retail and small business customers		518,306
Less stable deposits from retail and small business customers		735,698
Operational deposits		189,482
Other wholesale funding		1,754,008
Other liabilities		106,770
Total available stable funding		3,626,158
HQLA		439,461
Alternative liquid assets (ALA)		224,200
RBNZ securities		17,363
Loans to financial institutions		297,870
Residential mortgages with a risk weight equal to 35%		1,324,569
Other loans		1,096,529
Non-HQLA exchange traded equities & securities & physical traded commodities		45,387
Other assets		186,942
Off-balance sheet items		709,697
Total required stable funding		4,342,018
NSFR		112.5%

<sup>1</sup> Total exposures have been calculated as the leverage ratio exposure measure for IRB ADIs and total assets for other ADIs. The leverage ratio exposure measure for one ADI as at September 2018 has been included, since the amount as at December 2018 is yet to be reported.

<sup>2</sup> APRA has alternative quantitative liquidity standards for small, less complex, locally incorporated ADIs and for foreign bank branches. The qualitative requirements in APS 210, which are formulated in line with the BCBS Principles for Sound Liquidity Risk Management and Supervision, are applicable to all ADIs.

Source: APRA.

## Annex 4: Materiality assessment

The outcome of the RCAP assessment is based on the materiality of the findings described in Section 2.2 and summarised in Table A.3. Assessment Teams evaluate the materiality of findings quantitatively where possible, or using expert judgment when the impact cannot be quantified.

The materiality assessment for quantifiable gaps is based on the cumulative impact of the identified deviations on the reported NSFRs of banks in the RCAP sample. These banks are listed in Table A.4.

Number of deviations by component				Table A.3
Component	Not material	Potentially material	Material	
Scope, minimum requirement and application issues	0	0	0	
Available stable funding (numerator)	1	0	0	
Required stable funding (denominator)	0	0	0	
NSFR disclosure requirements	1	0	0	

RCAP sample banks		Table A.4
Banking group	Share of banks' assets in the total assets of the Australian banking system (per cent)	
Bank 1	19.6%	
Bank 2	20.2%	
Bank 3	18.4%	
Bank 4	18.5%	
Bank 5	4.3%	
Total	80.9%	

Source: APRA. For this purpose, banking assets are based on the measure of total exposures used in the leverage ratio, which includes both on- and off-balance sheet exposures.

## Annex 5: Areas where APRA's rules are stricter than the Basel standards

In some areas, the Australian authorities have adopted a stricter approach than the minimum standards prescribed by the Basel Committee. These are listed below for information. The stricter rules have not been taken into account as mitigants for the overall or component-level assessment of compliance.

- For ASF purposes, the Basel standard provides that, for funding with options exercisable at the bank's discretion, supervisors should take into account reputational factors that may limit a bank's ability not to exercise the option, particularly where the market expects certain liabilities to be redeemed before their legal final maturity date. APRA requires an ADI to assume that it will redeem a funding instrument with a call option at the earliest possible date, regardless of investors' expectations (Basel paragraph 18). This is similarly applied on the asset side for RSF purposes. The Basel standard provides that, for assets with options exercisable at the bank's discretion, supervisors should take into account reputational factors that may limit a bank's ability not to exercise the option, particularly where the market expects certain assets to be extended in their maturity. APRA also requires an ADI to assume that it will exercise an option to extend the maturity of an asset, regardless of market expectations (Basel paragraph 29).
- The Basel NSFR standard assigns a 20% RSF factor on derivative liabilities. At national discretion, jurisdictions may lower the value of this factor, with a floor of 5%. APRA applies a 20% RSF factor on gross derivatives liabilities. APRA does not have any plans to modify the 20% RSF factor on gross derivative liabilities and apply a lower RSF factor in accordance with national discretion.
- The Basel standard requires application of the NSFR to all internationally active banks on a consolidated basis. APRA is more rigorous in terms of the scope of application in two aspects. It applies the NSFR at both the bank and consolidated level and in addition it applies the NSFR to all Australian banks that are subject to the LCR, not just those that are internationally active.

## Annex 6: Elements of the NSFR subject to national discretion

The following table provides information on elements of NSFR implementation that are subject to prudential judgment and national discretion. The information provided helps the Basel Committee to identify implementation issues where clarifications and (additional) FAQs could improve the quality and consistency of implementation. It should also inform the preliminary design of any peer comparison of consistency across the membership that the Committee may decide to conduct, in similar fashion to the studies on risk-weighted asset variation for the capital standards.

Implementation of national discretions by APRA

Table A.5

Basel paragraph	Description	National implementation
25(a)	Treatment of deposits between banks within the same cooperative network	Subject to APRA's approval, deposits between ADIs within the same cooperative network may be excluded from liabilities receiving zero percent ASF, subject to certain conditions. Currently, there are no NSFR ADIs that operate within a cooperative network. APRA rules (APS 210 Att. C par 15 and footnote 18) which included an approval process could raise an issue on the consistency of application across covered institutions. Nonetheless, APRA represented that it has not approved any cooperative network deposits for an ASF factor that is higher than zero percent.
31	Treatment of excess collateral in a covered bond collateral pool allowing for multiple issuance	APRA adopted Basel NSFR FAQ 34 issued in February 2017. This can be generally referenced to APRA Liquidity FAQ 11 published on its website. In essence, APRA states that the Basel FAQs are not in conflict with its standards and in the event that the ADI is uncertain, the latter should contact APRA.
31, 36	Treatment of central bank operations	(Basel standard 31) exceptional liquidity operations Subject to APRA's approval, an asset encumbered to exceptional central bank liquidity operations may be assigned with a lower RSF factor.  (Basel standard 31) derivatives transactions with central banks arising from short-term monetary policy and liquidity operations APRA adopted Basel NSFR FAQ 33 issued in February 2017. This can be generally referenced to APRA Liquidity FAQ 11 published on its website. In essence, APRA states that the Basel FAQs are not in conflict with its standards and in the event that the ADI is uncertain, the latter should contact APRA.  (Basel standard 36) central bank reserves An RSF factor of zero percent applies to central bank reserves. However, APRA has the discretion to impose a higher RSF factor after discussing and agreeing with the relevant central bank and considering whether the reserve requirement in a particular jurisdiction requires associated stable funding.
43	RSF factor for derivative liabilities	APRA did not exercise national discretion. APRA has no plans to modify the 20% RSF factor on derivatives liabilities and apply a lower RSF factor in accordance with national discretion.
45	Treatment of interdependent assets and liabilities	APRA may determine in exceptional circumstances that certain assets and liabilities are interdependent and adjust their RSF and ASF factors to zero, subject to certain criteria. At this time, APRA has not identified any circumstances warranting interdependent treatment.

47	RSF factors for other contingent funding obligations	<p>An RSF factor of 1% applies to unconditionally revocable credit and liquidity facilities. An RSF factor of 100% applies to the actual net outflows in the most recent 12-month period for trade finance-related obligations and guarantees and letters of credit unrelated to trade finance obligations.</p> <p>APRA rules do not specifically identify non-contractual obligations among the off-balance sheet items.</p>
50	Scope of application of NSFR and scope of consolidation of entities within a banking group	NSFR is applied to all locally incorporated LCR ADIs on both solo and consolidated bases. This includes all internationally active ADIs and other smaller ADIs which only have domestic operations and the Australian subsidiaries of foreign banks. Branches of foreign banks are not subject to the NSFR.

Source: APRA.

## Annex 7: RCAP-LCR follow-up: host jurisdiction securities in HQLA

The October 2017 RCAP of the Australian LCR highlighted the issue of the inclusion of Reserve Bank of New Zealand (RBNZ) securities as Level 1 HQLA. While the overall grade was compliant, the HQLA component grade was assigned as largely compliant, due primarily to the materiality of including RBNZ securities in HQLA. The inclusion of RBNZ securities as Level 1 HQLA inflated the overall industry LCR by 4.3%.

Per the RCAP-LCR report, the Basel Committee asked the Working Group on Liquidity (WGL) to consider the issue of treatment of assets to cover net cash outflows in ALA countries or non-BCBS countries. In the Basel LCR standard there is only one provision for using a host jurisdiction's liquidity parameters and it concerns the definition of retail/small business, not HQLA (see Basel LCR paragraph 169). The issue addressed by the WGL is that RBNZ securities do not meet the requirements for Level 1 HQLA in the Basel LCR standard and there is no provision to use host (New Zealand) liquidity parameters for HQLA.

The WGL conducted an internal survey of WGL members to determine the scope of the issue and found that few members have similar issues. As such, the WGL recommended addressing the issue through internal guidance. The internal guidance developed by the WGL was reviewed and approved by the PDG and SIG. The guidance allows the inclusion of HQLA recognised in these jurisdictions in the calculation of the LCR up to the amount of the bank's net cash outflows in a stress scenario as specified in paragraph 19 for the subsequent 30 days. Any such HQLA held in excess of the net cash outflows stemming from and in the currency of that jurisdiction must be excluded from the LCR. The APRA LCR regulation does not contain this limitation on host securities HQLA.

Based on the data submitted as part of the 2017 RCAP-LCR, NZD net cash outflows comprise 0–15% of each sample ADI's total net cash outflows or 7.6% on average. The ADI with the largest NZD net cash outflows does not hold total NZD HQLA (ie NZ government securities, Reserve Bank of NZ bills and other RBNZ eligible securities) in excess of total NZD net cash outflows. The NZD HQLA in excess of NZD net cash outflows represents approximately 1–2% of the total all-currency HQLA at these ADIs.

APRA's response to this finding in the RCAP-LCR was that it "is awaiting further guidance from the Basel Committee on this issue, after which it will review its prudential requirements". Having now seen the internal guidance, APRA informed the Assessment Team that it had communicated to its banks that no RBNZ securities above the amount of stressed outflows could be included in HQLA. The Assessment Team confirmed with the Australian banks that the guidance had been communicated. Australian banks have implemented the guidance and now report their LCRs in accordance with it.