



29 March 2016

To: All authorised deposit-taking institutions (ADIs), general insurers, life companies, Level 2 Heads and potential Level 3 Heads

APRA is today announcing two measures in relation to the implementation of its framework for the supervision of conglomerate groups (Level 3 framework).

By way of background, APRA released the Level 3 framework¹ in August 2014, but did not set an implementation date for the new requirements as the Financial System Inquiry (FSI) was reviewing the financial services regulatory regime more broadly. APRA considered it appropriate to await the findings of the FSI, and the Government's response to its recommendations, before settling on the final form of the Level 3 framework.

APRA is today advising regulated institutions of a revised implementation timetable for the Level 3 framework, taking into account the FSI's recommendations.

1. Release of the non-capital components of the framework for supervision of conglomerate groups

APRA is today releasing for consultation clarifications to the non-capital components of the Level 3 framework. This includes nine prudential standards and two prudential practice guides. It is intended that these will become effective on 1 July 2017.

Prudential standards and prudential practice guides applicable to Level 3 Heads

- *Prudential Standard 3PS 001 Definitions*
- *Prudential Standard 3PS 221 Aggregate Risk Exposures*
- *Prudential Standard 3PS 222 Intra-group Transactions and Exposures*
- *Prudential Standard 3PS 310 Audit and Related Matters*
- *Draft Prudential Practice Guide 3PG 221 Aggregate Risk Exposures*
- *Draft Prudential Practice Guide 3PG 222 Intra-group Transactions and Exposures*

Prudential standards applicable to ADIs, general insurers, life companies, Level 2 Heads and Level 3 Heads

- *Prudential Standard CPS 220 Risk Management*
- *Prudential Standard CPS 231 Outsourcing*
- *Prudential Standard CPS 232 Business Continuity Management*
- *Prudential Standard CPS 510 Governance*
- *Prudential Standard CPS 520 Fit and Proper*

The clarifications to the cross-industry (CPS) standards largely relate to their application to Level 3 Heads and Level 2 Heads. However, as these standards also apply to all ADIs, general

¹ http://www.apra.gov.au/MediaReleases/Pages/14_15.aspx

insurers and life companies, APRA considers it is important for all entities to review the clarifications to these prudential standards.

2. Deferral of the capital components of the Level 3 framework

In order to allow the form of the final capital requirements to be determined following the finalisation of other domestic and international policy initiatives that are already in progress, APRA considers that it is appropriate to defer finalising the capital components of the Level 3 framework at this stage.

These policy initiatives include further developments regarding APRA's implementation of the FSI recommendation on unquestionably strong capital ratios for ADIs (FSI recommendation 1), consideration of proposals in relation to loss absorption and recapitalisation capacity (FSI recommendation 3); proposed legislative changes to strengthen APRA's crisis management powers (FSI recommendation 5). Taken together, these initiatives will influence APRA's final views on the appropriate requirements with respect to the strength, resilience, recovery and resolution capacity of conglomerate groups.

APRA intends to consult again on the capital requirements in the Level 3 framework but, in light of the need to finalise these other policy initiatives as a matter of priority, does not anticipate that this consultation will commence earlier than mid-2017. Implementation of any new requirements will therefore be no earlier than 2019.

Invitation to comment on clarifications to the non-capital Level 3 prudential standards - due Friday 13th May

As a result of APRA's decision to defer finalising the capital components of the Level 3 framework, it has been necessary to make some adjustments and clarifications to the prudential standards that are being released today for consultation. These clarifications, which are set out in more detail in the Attachment to this letter, are:

- edits necessary as a result of *Prudential Standard 3PS 110 Capital Adequacy* (3PS 110) not being finalised at this time;
- drafting clarifications regarding the requirements for a Head of a group in the cross-industry prudential standards;
- edits to address feedback provided in submissions to APRA's consultation on *Improving APRA's board engagement* in October 2014, to improve the clarity of the requirements applying to a Board; and
- an amendment in *Prudential Standard CPS 220 Risk Management* (CPS 220) to the timeline for submitting a risk management declaration to APRA in response to feedback from industry that the existing wording created some confusion.

In addition, 3PS 110 included limitations on the activities of a non-operating holding company (NOHC) that is a Level 3 Head. As 3PS 110 is not being finalised, APRA intends to implement these limitations by way of updates to the authorisation conditions for each NOHC that is a Level 3 Head.

These clarifications are intended to reflect necessary changes to implement the non-capital components of the Level 3 framework, and are generally not intended to change previously settled policy positions. However, the amendment to the risk management declaration submission timeline in CPS 220 may be a change in regulatory requirements for some entities. This change has been made to remove inconsistencies, and in response to industry queries on this matter.

Invitation for submissions on draft non-capital Level 3 prudential practice guides - due Friday 27th May

APRA has also today released for consultation two prudential practice guides. Whilst these were published in August 2014, they have not been consulted on previously. Submissions on the prudential practice guides should be provided by Friday 27th May.

Submissions on the clarifications to the prudential standards and/or the draft prudential practice guides should be provided by email to Level3Framework@apra.gov.au by the dates indicated above, and addressed to

Mr Pat Brennan
General Manager, Policy Development
Policy and Advice Division
Australian Prudential Regulation Authority

Yours sincerely

A handwritten signature in dark ink, appearing to read 'Byres', with a stylized flourish at the end.

Wayne Byres
Chairman

Attachment - Key clarifications to the draft prudential standards

3PS 001

- Definitions that are not used beyond the capital components of the Level 3 framework have been removed;
- definitions of Level 3 group and Level 3 Head have been moved from 3PS 110 into the definitions standard; and
- some definitions updated to improve clarity.

Note: APRA is considering issuing a consolidated definitions standard that would combine *Prudential Standard APS 001 Definitions*, *Prudential Standard GPS 001 Definitions*, *Prudential Standard LPS 001 Definitions* and *Prudential Standard 3PS 001 Definitions* and will consult on this proposal in due course.

3PS 221 and 3PS 222

- Consequential changes as 3PS 110 is not being released; and
- clarification of Board requirements.

3PS 310

- Consequential changes as there are no Level 3 reporting forms at this stage; and
- clarification of use of separate auditors.

CPS 220

- The current version of CPS 220 already includes Level 3 requirements; these have been updated as 3PS 110 is not being released;
- clarification of how the requirements apply to a Head of a group, to more clearly articulate the requirements on a group basis, including where the Head of the group is not required to duplicate notification requirements fulfilled by APRA-regulated institutions within the group; and
- an amendment to the timeline for submitting a risk management declaration to APRA in response to feedback from industry that the current wording created some confusion.

CPS 231 and CPS 232

- The current versions of CPS 231 and CPS 232 have not incorporated the Level 3 amendments announced in August 2014. These are included in the versions released today as tracked changes (highlighted in yellow to differentiate them from the newer changes). APRA does not expect comments on these words as they were previously finalised following consultation;
- clarification of how the requirements apply to a Head of a group, to more clearly articulate the requirements on a group basis, including where the Head of the group is not required to duplicate notification requirements fulfilled by APRA-regulated institutions within the group; and
- clarification of Board requirements in response to issues raised in submissions to APRA's consultation on *Improving APRA's board engagement* in October 2014 (highlighted in blue).

CPS 510

- The current version of CPS 510 already includes Level 3 requirements; these have been updated as 3PS 110 is not being released;
- clarification of how the requirements apply to a Head of a group, to more clearly articulate the requirements on a group basis; and
- clarification of Board requirements in response to issues raised in submissions to APRA's consultation on *Improving APRA's board engagement* in October 2014 (highlighted in blue).

CPS 520

- The current version of CPS 520 has not incorporated the Level 3 amendments announced in August 2014. These are included in the version released today as tracked changes (highlighted in yellow to differentiate them from the newer changes). APRA does not expect comments on these words as they were previously finalised following consultation; and
- clarification of how the requirements apply to a Head of a group, to more clearly articulate the requirements on a group basis, including where the Head of the group is not required to duplicate notification requirements fulfilled by APRA-regulated institutions within the group.