

Australian Prudential Regulation Authority instrument fixing charges No. 2 of 2022

Models-based capital adequacy requirements for ADIs for the financial year 2021-22

EXPLANATORY STATEMENT

Issued by the Australian Prudential Regulation Authority (*APRA*)

Australian Prudential Regulation Authority Act 1998, paragraphs 51(1)(a) and (b)

Instrument to which this Explanatory Statement relates

This Explanatory Statement relates to Australian Prudential Regulation Authority instrument fixing charges No. 2 of 2022 which is made under paragraphs 51(1)(a) and (b) of the *Australian Prudential Regulation Act 1998* (the ***APRA Act***) and dated 28 June 2022 (the ***instrument***).

1. Background

Legislative framework

APRA has statutory responsibility for the prudential supervision of most of the superannuation industry, the life, general and private health insurance industries, and authorised deposit-taking institutions (**ADIs**). ADIs include banks, building societies and credit unions.

Subsection 51(1) of the APRA Act provides that APRA may, by legislative instrument, fix charges to be paid to it by a person in respect of:

- (a) services and facilities APRA provides the person; or
- (b) applications or requests (however described) made to APRA under any law of the Commonwealth.

Subsection 51(2) of the APRA Act provides that a charge fixed under subsection 51(1) must be reasonably related to the costs incurred or to be incurred by APRA in relation to the matters to which the charge relates and must not be such as to amount to taxation.

Purpose and operation of the instrument

The instrument imposes a charge for certain services provided by APRA relating to the ongoing supervision of the capital adequacy of banks which have adopted the models-based approach under the Basel Capital Framework (***Basel II***) for ADIs to determine their capital adequacy requirements and to the accreditation of other ADIs which have applied to APRA for accreditation to use that approach.

Factual background

In June 2004, the Basel Committee on Banking Supervision (the **Committee**) released Basel II, reforming the 1988 Basel Capital Accord (the **1988 Accord**).

APRA implemented Basel II in Australia for all ADIs on 1 January 2008, through new prudential standards under section 11AF of the *Banking Act 1959*. Under these standards, ADIs are able to determine their capital adequacy requirements using one of two methods:

- a) a standardised (default) method (the **standardised method**); or
- b) a models-based approach that more closely aligns with an ADI's individual risk profile (the **models-based approach**).

ADIs seeking to use the models-based approach must have APRA's approval to do so.

Basis of charging

APRA is principally funded by the annual supervisory levy imposed by the *Financial Institutions Supervisory Levies Collection Act 1998* and the related levy imposition Acts. However, section 51 of the APRA Act empowers APRA to impose charges in respect of services or facilities provided by it and in respect of applications or requests made to it under any law of the Commonwealth.

Underlying section 51 is the principle of 'user pays' – that parties who receive special services or benefits from APRA should, where appropriate, have to pay the cost of APRA providing these special services or benefits, rather than leaving them to be funded out of the supervisory levy which is paid by the general body of regulated institutions. APRA continues to charge fees that recover the assessment cost for, and ongoing supervision of, those ADIs seeking Basel II accreditation.

How the charges have been calculated

The charges set by the instrument are fixed on a cost recovery basis and in line with the *Australian Government Cost Recovery Guidelines July 2014 – Resource Management Guide No. 304*.

The charge is based on the need to recover APRA's costs of ongoing monitoring of the capital adequacy of ADIs using the models-based approach, assessing applications from ADIs seeking to use this approach and performing policy development relating to revisions to the models-based approach. Those costs are based on an estimation of APRA staff time involved with an addition of direct overhead costs. On this basis, APRA's total cost recovery in respect of the models-based approach for 2021-22 is \$2.73 million (2020-21: \$1.63 million).

The costs incurred in monitoring the capital adequacy of ADIs using the standardised method are recovered through financial sector levies.

In 2021-22, the focus has been on the ongoing supervision of the capital adequacy of ADIs approved to use, or are seeking approval to use, the models-based approach (Australia and New Zealand Banking Group Limited (**ANZ**), Commonwealth Bank of Australia (**CBA**), National Australia Bank Limited (**NAB**), Westpac Banking Corporation (**WBC**),

Macquarie Bank Limited (**MBL**), ING Bank (Australia) Limited (**ING**) and Bendigo and Adelaide Bank Limited (**BEN**).

As there is no material difference in APRA's approach to the monitoring of the models-based approach among the top six ADIs who have received approval, each of these will be charged an equal amount of the relevant costs. BEN is in the process of accreditation and does not benefit at this point. BEN is also charged lower than the six ADIs that were accredited to use models for the full year.

2. Operation of the instrument

Description of the charges

The charge imposed by the instrument is based on a two-tiered structure:

- (a) \$442,000 plus GST (which totals \$486,200) for ANZ, CBA, NAB, WBC, MBL and ING; and
- (b) \$75,000 plus GST (which totals \$82,500) for BEN.

Charges must be reasonably related to the costs and expenses incurred

As indicated above, the charges set by the instrument are fixed on a cost recovery basis to recover the estimated effort involved in the discharge of APRA's responsibilities and in line with the *Australian Government Cost Recovery Guidelines July 2014*.

Cost Recovery Implementation Statement

A Cost Recovery Implementation Statement (CRIS) has been tabled in support of this Explanatory Statement and will be published on the APRA website prior to invoicing.

Charges must not amount to taxation

As disclosed in the accompanying CRIS, the charges are reasonably related to the costs incurred by APRA in providing the services concerned and therefore do not constitute a tax.

3. Consultation

As required under section 17 of the *Legislation Act 2003*, before a legislative instrument is made, appropriate consultation must be undertaken with those persons who are likely to be affected by the proposed instrument. APRA consulted with the ADIs before making this legislative instrument. The relevant officers of all the ADIs were advised by email of APRA's intention to recover the costs of the ongoing supervision and accreditation work. The advice provided an invitation to the ADIs to raise any questions or concerns. The consulted roles in the ADIs included:

Consulted entity	Consulted role
Australia and New Zealand Banking Group Limited	GGM Risk Metrics and Measurement
Commonwealth Bank of Australia	Head of the APRA Portfolio Relationship team
National Australia Bank Limited	Head of Regulatory Affairs, Prudential & BEAR
Westpac Banking Corporation	Chief Executive Officer
Macquarie Bank Limited	Executive Director

ING Bank (Australia) Limited	Chief Financial Officer
Bendigo and Adelaide Bank Limited	Chief Risk Officer

During the consultation process, the ADIs did not raise any objections to the charges being applied.

4. Statement of Compatibility prepared in accordance with Part 3 of the Human Rights (Parliamentary Scrutiny) Act 2011

A Statement of Compatibility prepared in accordance with Part 3 of the *Human Rights (Parliamentary Scrutiny) Act 2011* is provided at Attachment A to this Explanatory Statement.

Attachment A**Statement of Compatibility with Human Rights**

Prepared in accordance with Part 3 of the *Human Rights (Parliamentary Scrutiny) Act 2011* (HRPS Act)

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This Legislative Instrument is compatible with the human rights and freedoms recognised or declared in the international instruments listed in subsection 3(1) of the HRPS Act.

Overview of the Legislative Instrument

This Legislative Instrument will fix charges to be paid to APRA by authorised deposit-taking institutions (ADIs) for specific costs associated with the supervision of the capital adequacy of ADIs using a model-based approach and assessing applications by ADIs to use the models-based approach.

Human rights implications

APRA has assessed this Legislative Instrument against the international instruments listed in subsection 3(1) of the HRPS Act and determined that this Legislative Instrument does not engage any of the applicable rights or freedoms, as the charges payable by the ADIs will not have any direct or indirect effect on the rights of individual persons.

Conclusion

Australian Prudential Regulation Authority instrument fixing charges No. 2 of 2022 is compatible with human rights as it does not raise any human rights issues.