# Banking (prudential standard) determination No. 1 of 2025

# EXPLANATORY STATEMENT

# Prepared by the Australian Prudential Regulation Authority (APRA)

# *Banking Act 1959*, section 11AF

Under subsection 11AF(1) of the *Banking Act 1959* (the Act), APRA has the power to determine standards (prudential standards), in writing, in relation to prudential matters to be complied with by authorised deposit-taking institutions (ADIs) and authorised non-operating holding companies (authorised NOHCs). Under subsection 11AF(3) of the Act, APRA may, in writing, vary or revoke a prudential standard.

On 13 April 2025, APRA made Banking (prudential standard) determination No. 1 of 2025 (the instrument), which revokes *Prudential Standard APS 111 Capital Adequacy: Measurement of Capital* made under Banking (prudential standard) determination No. 5 of 2022 and determines a new *Prudential Standard* *APS 111 Capital Adequacy: Measurement of Capital* (APS 111).

The instrument commences on 1 July 2025.

## Background

APRA’s mandate is to ensure the safety and soundness of prudentially regulated financial institutions so that they can meet their financial promises to depositors, policyholders, and fund members within a stable, efficient, and competitive financial system.

APRA carries out this mandate through a multi-layered prudential framework that encompasses licensing and supervision of institutions. In the case of the banking industry, APRA is empowered under the Act to issue legally binding prudential standards that set out specific prudential requirements with which ADIs must comply.

APRA regularly reviews its regulatory regime and amends its prudential requirements as a result of a number of factors, including:

* international developments;
* changes in financial market conditions or changes in risk management practices, in response to identified weaknesses in the prudential framework; and
* to reduce potential negative impacts of emerging industry issues.

A key component of APRA’s prudential framework is the suite of prudential standards that impose regulatory capital requirements on ADIs for the purpose of ensuring ADIs hold sufficient capital to address the risks associated with their operations. One of these capital standards is APS 111.

APS 111 supports *Prudential Standard APS 110 Capital Adequacy* (APS 110), the latter standard requiring an ADI to maintain required levels of regulatory capital.

As Australia is a member of the Basel Committee on Banking Supervision (BCBS) and the Group of 20, Australia and APRA are committed to meeting internationally agreed standards for prudential regulation for ADIs by implementing capital standards that are based on the framework agreed by the BCBS. APS 111 follows closely the BCBS’s definition of capital standard, with appropriate Australian adjustments.

## Purpose and operation of the instrument

The purpose of the instrument is to revoke the existing APS 111 and replace it with a new version of APS 111.

APS 111 sets out the characteristics that an instrument must have to qualify as regulatory capital and the various deductions to be made to determine total regulatory capital on both a Level 1 (ADI) and Level 2 (banking group) basis.

The new APS 111 incorporates amendments resulting from APRA’s targeted changes to strengthen liquidity and capital requirements for ADIs, specifically policy changes on market valuations for liquid assets.[[1]](#footnote-2) The new APS 111:

* includes a definition of ‘fair value’ which has the meaning given in the Australian Accounting Standards;
* requires that an ADI must deduct from Common Equity Tier 1 Capital at Level 1 and Level 2 the amount of the cumulative unrealised fair value losses for liquid assets that it does not measure at fair value; and
* clarifies that an ADI may deduct unrealised fair value losses at a portfolio level so that unrealised fair value gains on liquid assets can offset unrealised fair value losses at a financial instrument level.

### Details of the new prudential standard

See Attachment A.

### Documents incorporated by reference

Under paragraph 14(1)(a) of the *Legislation Act 2003*, the standard incorporates by reference as in force from time to time:

* Acts of Parliament and associated delegated laws;
* Prudential Standards determined by APRA under subsection 11AF(1) of the Act;
* the Australian Accounting Standards determined by the Australian Accounting Standards Board under section 334 of the *Corporations Act 2001* (Cth); and
* the Australian Auditing Standards determined by the Auditing and Assurance Standards Board under section 336 of the *Corporations Act 2001* (Cth).

These documents may be freely obtained on the Federal Register of Legislation at www.legislation.gov.au (all documents listed above except for Australian Accounting and Auditing Standards), https://www.aasb.gov.au/pronouncements/accounting-standards/ (Australian Accounting Standards) and https://auasb.gov.au/standards-guidance/auasb-standards/auditing-standards/ (Australian Auditing Standards).

Under paragraph 14(1)(b) of the *Legislation Act 2003*, the standard incorporates by reference as existing at the commencement of the standard:

* Principles on Loss-absorbing and Recapitalisation capacity of G-SIBs in Resolution issued by the Financial Stability Board on 9 November 2015, which may be freely obtained at www.fsb.org/2015/11/total-loss-absorbing-capacity-tlac-principles-and-term-sheet/.

### Exercise of discretion by APRA

Under subsection 11AF(2) of the Act, a prudential standard may provide for APRA to exercise powers and discretions under the standard, including (but not limited to) discretions to approve, impose, adjust or exclude specific prudential requirements in relation to one or more specified ADIs or authorised NOHCs.

APRA’s prudential standards include powers that may be exercised by APRA that involve an element of discretion and that may affect the interests of the ADIs to which the prudential standards apply. These powers include a power to adjust or exclude a provision of the prudential standard.

The need to apply discretion is driven by entity-specific issues and circumstances that are not adequately addressed by the generally applicable provisions of the prudential standards. For example, adjustment or exclusion of a provision may be necessary to obtain a better prudential outcome than would be the case if the prudential requirement were applied unaltered to a particular regulated entity.

When exercising its discretion, APRA considers a wide range of factors, including the considerations set out in the Act and the *Australian Prudential Regulation Authority Act 1998*.

The exercise of APRA's powers is governed by a robust decision-making framework which is documented in APRA's internal policies. This framework supports APRA in fulfilling its mandate by limiting decision making to those senior APRA officers with the appropriate experience and skill to exercise prudent judgement. The framework also requires decision makers to seek advice from internal technical experts.

The power is also exercised following discussion with the relevant ADI about its appropriateness and the impact it may have on the entity.

### Review of decisions

Decisions made by APRA exercising powers in prudential standards are not themselves subject to merits review. This is because these decisions are preliminary decisions that may facilitate or lead to substantive decisions which are subject to merits review.

A breach of a prudential standard is a breach of the Act, as section 11AG of the Act provides that ADIs must comply with applicable prudential standards. However, there are no penalties prescribed for such breaches. Instead, an ADI’s breach of a provision in the Act is grounds for APRA to make further, substantive decisions under the Act in relation to the ADI. Those decisions are:

* to revoke an authority to carry on banking business (section 9A of the Act); and
* to issue a direction to the ADI, including a direction to comply with the whole or part of a prudential standard (section 11CA of the Act).

It is only at this stage that an ADI is exposed to a penalty: loss of its authority under section 9A or 50 penalty units if it breaches the direction (section 11CG of the Act). In nearly all cases[[2]](#footnote-3) the decision is preceded by a full consultation with the ADI to raise any concerns it may have in relation to the decision.

A decision of APRA to impose a direction is subject to merits review under section 11CA of the Act, which is appropriately available at the point where an ADI could be exposed to a penalty.

A decision of APRA to revoke an authority under the Act is subject to merits review, unless either:

1. APRA has determined that access to natural justice and merits review is contrary to the national interest or contrary to the interests of depositors with the ADI; or
2. the authority is an authority that is to cease to have effect on a day specified in the authority (section 9A(8) of the Act).

## Consultation

In November 2023, APRA released proposed targeted changes to liquidity requirements for consultation.[[3]](#footnote-4) The changes primarily affect smaller ADIs on the Minimum Liquidity Holdings (MLH) regime and aim to strengthen the banking sector’s resilience to future stress.

The consultation closed on 16 February 2024, with 35 submissions provided by industry. APRA also held numerous workshops with industry bodies and bilateral meetings with entities. Industry generally supported APRA’s efforts to uplift valuation practices.

In July 2024, APRA issued a response paper that set out APRA’s response to submissions, the final APS 210 and consequential changes to APS 111.

APRA is satisfied the consultation was appropriate and reasonably practicable.

## Impact Analysis

The Office of Impact Assessment (OIA) confirmed a Regulatory Impact Statement was not required.

## 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 B to this Explanatory Statement.

**ATTACHMENT A**

**Details of the new prudential standard**

Authority and application

Under subsection 11AF(1) of the Act, APRA may determine prudential standards to be complied with by (among others) all, or specified classes of, ADIs and authorised NOHCs.

Paragraphs 1 to 5 are the machinery provisions relating to the legal authority under which the instrument is made, and the classes of ADIs and authorised NOHCs that are required to comply with the standard.

Commencement

Paragraph 6 is a machinery provision relating to the commencement of the standard.

Adjustments and exclusions

Paragraph 7 relies on subsection 11AF(2) of the Act and provides for APRA to adjust or exclude a specific requirement in APS 111 in relation to one or more specified ADIs or authorised NOHCs.

Previous exercise of discretion

Paragraph 8 requires an ADI to contact APRA if it intends to rely on a previous exemption of a prudential requirement, or other exercise of discretion, provided by APRA under a previous version of APS 111.

Interpretation

Paragraph 9 is a machinery provision and notes that terms that are defined in *Prudential Standard CPS 001 Defined terms* appear in bold the first time they are used in APS 111. This paragraph also notes that a reference to an Act, Regulations, Prudential Standard, Australian Accounting Standard or Australian Auditing and Assurance Standard in APS 111 is a reference to the instrument as in force from time to time.

Definitions

Paragraph 10 is a machinery provision setting out relevant definitions.

Regulatory Capital

Paragraphs 11 to 28 describe each component and category of regulatory capital, and the criteria that must be satisfied to include in total regulatory capital.

These paragraphs also outline the circumstances where APRA may require an ADI to exclude from regulatory capital any item included as a component of capital or reallocate to a lower category of regulatory capital any component of capital.

Further, these paragraphs state a capital instrument is not eligible for inclusion in regulatory capital if it contains any terms that could inhibit the ADI’s ability to be managed in a sound and prudent manner, particularly in times of financial difficulty, or restrict APRA’s ability in its role as prudential regulator to resolve any problems encountered by the ADI.

In addition, these paragraphs outline documentation and consultation requirements associated with the issue of a capital instrument, and APRA’s approval before the terms of an instrument are altered in a way that may affect its eligibility as regulatory capital.

Application of fair values

Paragraph 29 provides that where an ADI measures its financial instruments at fair value for capital adequacy purposes, and where permitted, for other prudential purposes, it must comply with the requirements in Attachment A to APS 111.

Common Equity Tier 1 capital

Paragraphs 30 to 38 outline the characteristics that fully satisfy Common Equity Tier 1 (CET1) capital.

CET1 capital is the highest quality of regulatory capital, as it absorbs losses immediately when they occur.

Additional Tier 1 capital

Paragraphs 39 to 40 outline the characteristics that fully satisfy Additional Tier 1 capital.

Along with CET1 capital, Additional Tier 1 capital provides loss absorption on a going-concern basis, although Additional Tier 1 capital instruments do not meet all the criteria for CET1 capital.

Tier 2 capital

Paragraphs 41 to 44 outline the characteristics that fully satisfy Tier 2 capital.

Tier 2 capital is gone-concern capital. That is, when an ADI fails, Tier 2 instruments must absorb losses before depositors and general creditors do.

Additional Tier 1 capital or Tier 2 capital issued overseas by ADIs or subsidiaries

Paragraph 45 outlines the circumstances where Additional Tier 1 capital or Tier 2 capital issued overseas by ADIs, or subsidiaries may be recognised in regulatory capital.

Intra-group capital transactions

Paragraphs 46 to 48 outline the matters APRA may consider in assessing whether an item included by an ADI as a component of capital resulting from intra-group transactions is not a genuine contribution to financial strength.

Holding of capital instruments in group members by other group members

Paragraph 49 sets out the circumstances where holdings of capital instruments in group members by other group members may be included in regulatory capital.

Paragraph 50 describes the circumstances where direct investments in shares of an ADI by a special purpose vehicle established under a share-based employee remuneration scheme may be included in the ADI’s CET1 capital.

Paragraph 51 states that a capital instrument must be treated as holdings of own capital instruments and deducted, as appropriate, if requirements in paragraphs 49 and 50 are not met.

Attachment A - Use of Fair Values

Attachment A of APS 111 sets out the requirements for an ADI to measure its financial instruments at fair value for capital adequacy and, where permitted, for other stated prudential purposes referred to in other Prudential Standards.

Attachment B - Criteria for classification as paid-up ordinary shares

Attachment B of APS 111 sets out the criteria for an instrument to be classified as paid-up ordinary shares in CET1 capital.

Attachment C - Minority interest and other capital issued out of fully consolidated subsidiaries that is held by third parties

Attachment C of APS 111 sets out the requirements for minority interest and other capital issued out of fully consolidated subsidiaries that is held by third parties to be included in regulatory capital.

Attachment D - Regulatory adjustments

Attachment D of APS 111 sets out regulatory adjustments (i.e. deductions) from a category of an ADI’s regulatory capital that must be made to determine total regulatory capital.

These deductions typically address the high degree of uncertainty that these items have a positive realisable value in periods of stress and are mostly applied to CET1 capital.

Attachment E - Criteria for inclusion in Additional Tier 1 capital

Attachment E of APS 111 sets out the criteria for an instrument to be classified as Additional Tier 1 capital.

Attachment F - Loss absorption requirements: Additional Tier 1 capital

Attachment F of APS 111 sets out the requirements for an Additional Tier 1 capital instrument classified as ‘liabilities’ under Australian Accounting Standards to include a provision whereby upon the occurrence of a loss absorption event it will be immediately and irrevocably converted into CET1 capital or written off.

A loss absorption event occurs when the issuing ADI’s Level 1 or Level 2 CET1 capital ratio under APS 110 falls to, or below 5.125 per cent of total risk-weighted assets (the loss absorption trigger point).

Attachment G – Criteria for inclusion in Tier 2 capital

Attachment G of APS 111 sets out the criteria for an instrument to be included in Tier 2 capital.

Attachment H - Loss absorption at the point of non-viability: Additional Tier 1 and Tier 2 Capital instruments

Attachment H of APS 111 sets out requirements that all capital instruments must be able to fully absorb losses at the point of non-viability (PONV).

The PONV condition requires all Additional Tier 1 capital and Tier 2 capital instruments to be capable of being converted into CET1 capital or written off. The trigger for the conversion or write-off is the earlier of: (i) a decision by APRA that the conversion or write-off is necessary, given that the ADI is assessed to be non-viable; and (ii) a decision to inject public funds to prevent the ADI’s failure.

Attachment I - Mutual equity interests

Attachment I of APS 111 sets out the criteria for an instrument to be classified as a Mutual Equity Interest and eligible to be included in CET1 capital. These requirements provide for mutually owned ADIs to issue CET1-eligible capital instruments directly without jeopardising their mutual status.

**ATTACHMENT B**

**Statement of Compatibility with Human Rights**

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

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The legislative instrument is compatible with the human rights and freedoms recognised or declared in the international instruments listed in section 3 of the *Human Rights (Parliamentary Scrutiny) Act 2011* (HRPS Act).

**Overview of the Legislative Instrument**

The purpose of the legislative instrument is to revoke *Prudential Standard APS 111 Capital Adequacy: Measurement of Capital* and replace it with a new version of APS 111.

APS 111 sets out the characteristics that an instrument must have to qualify as regulatory capital to be maintained by an authorised deposit-taking institution (ADI) and the various deductions to be made to determine total regulatory capital. ADIs are bodies corporate that have been granted the authority, under the *Banking Act 1959*, to carry on banking business in Australia.

**Human rights implications**

APRA has assessed the legislative instrument and is of the view that it does not engage any of the applicable rights or freedoms recognised or declared in the international instruments listed in section 3 of the HRPS Act. Accordingly, in APRA’s assessment, the legislative instrument is compatible with human rights.

**Conclusion**

The legislative instrument is compatible with human rights as it does not raise any human rights issues.

1. As part of the changes to APS 210, Minimum Liquidity Holdings (MLH) ADIs are required to adjust the value of their liquid assets regularly for movements in market prices. Unrealised losses on liquid assets were a key source of stress for some US banks in 2023, resulting in less liquidity being available at a time when it was needed most. Changes to APS 210 ensure that ADIs’ liquidity portfolios are based on market valuations and able to be realised at those valuations when needed. Refer to ‘*APRA finalises targeted changes to strengthen banks’ liquidity and capital requirements’* dated 24 July 2024 and available on APRA’s website. [↑](#footnote-ref-2)
2. Subsection 9A(4) of the Act specifically provides that APRA does not need to consult where APRA is satisfied that doing so could result in a delay in revocation that would be:

   contrary to the national interest; or

   contrary to the interests of depositors with the ADI. [↑](#footnote-ref-3)
3. APRA letter ‘*Targeted changes to ADI liquidity and capital standards’* dated 15 November 2023 and available on APRA’s website. [↑](#footnote-ref-4)