

Life Insurance (prudential standard) determination No. 1 of 2026

EXPLANATORY STATEMENT

Prepared by the Australian Prudential Regulation Authority (APRA)

Life Insurance Act 1995, section 230A

Under subsection 230A(1) of the *Life Insurance Act 1995* (the Act), APRA has power to determine standards in relation to prudential matters (prudential standards) to be complied with by life companies (including friendly societies), and registered non-operating holding companies (registered life NOHCs), and subsidiaries of life companies and registered life NOHCs. Under subsection 230A(5) of the Act, APRA may vary or revoke a prudential standard.

On 29 April 2026, APRA made *Life Insurance (prudential standard) determination No. 1 of 2026* (the instrument), which revokes *Prudential Standard LPS 112 Capital Adequacy: Measurement of Capital* made under *Life Insurance (prudential standard) determination No. 1 of 2024* (the previous LPS 112) and determines a new *Prudential Standard LPS 112 Capital Adequacy: Measurement of Capital* (the new LPS 112).

The instrument commences on 1 July 2026.

1. 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 life insurance industry, APRA is empowered under the Act to issue legally binding prudential standards that set out specific prudential requirements with which relevant APRA-regulated institutions must comply. These standards are supported by prudential practice guides which clarify APRA's expectations with regard to prudential requirements.

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

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

When amending its prudential requirements APRA has regard to, amongst other things, the impact on industry in terms of both industry burden and matters of proportionality.

A key component of APRA's prudential framework for the life insurance industry is the suite of prudential standards that impose regulatory capital requirements on relevant APRA-regulated institutions for the purpose of ensuring that they hold sufficient capital to address the risks associated with their operations.

The previous LPS 112 was one of APRA's core prudential standards that imposed regulatory capital requirements on life companies, by setting out the minimum capital requirements for life companies (including friendly societies). The previous LPS 112, along with APRA's other core capital adequacy prudential standards, was designed to address Australian-specific risks and to ensure that life companies remain well-capitalised. APRA's capital standards have increased the financial strength of life companies and supported the resilience of the Australian financial system. This helps to protect policyholders, maintain market confidence and promote financial stability, especially during potential scenarios of financial stress.

In June 2025, APRA commenced a review of its capital framework for longevity products (including annuities), to support better retirement outcomes for Australians by fostering a more vibrant and competitive annuity market.

The review was consistent with the Government's objective of expanding options for retirees to manage longevity risk and was a key contribution to APRA's strategic objective of 'getting the balance right' by ensuring its regulation is efficient and proportionate. The initiative was designed to support the market for retirement income products, with the better alignment of APRA's capital settings with the long-term nature of longevity liabilities supporting greater innovation and competition in the market for longevity products and allowing life companies to offer retirees better retirement income solutions.

In April 2026, the previous LPS 112 was remade to incorporate reforms stemming from the review.

2. Purpose and operation of the instrument

The purpose of this instrument is to revoke the previous LPS 112 and replace it with the new LPS 112. The new LPS 112 amends the previous LPS 112 by incorporating changes arising out of APRA's review of its capital framework for longevity products. This includes introducing a new, optional way to calculate the illiquidity premium (the 'advanced illiquidity premium' or 'AILP'), which increases the discount rate that life companies use to calculate liabilities for longevity products under APRA's capital framework. The changes are expected to provide capital relief benefits and to reduce pro-cyclicality within the capital requirements.

Adequate capital is critical to protect policyholders. APRA sets requirements on minimum capital to ensure life companies can absorb unexpected losses in their business. This is a core tool of prudential regulation and supports system-level financial stability.

The overarching purpose of LPS 112 is to ensure that a life company holds adequate capital against the risks it faces. The prudential standard specifies both the amount and type of capital that must be held.

A description of the key provisions of the new LPS 112 is set out in Attachment A to this Explanatory Statement.

3. Scope of administrative powers

Exercise of discretion by APRA

The new LPS 112 provides for APRA to exercise various discretions. Decisions made by APRA in exercising the discretions are not 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.

Under the Act, a breach of a prudential standard is a breach of the Act, as the Act provides that regulated entities must comply with the requirements of a standard. However, there are no penalties prescribed for such breaches. Instead, a breach of a provision in the Act is grounds for APRA to make further, substantive decisions under the Act in relation to the relevant entity. Those decisions may include the decision:

- (a) to issue a direction to the entity, including a direction to comply with the whole or part of a prudential standard (section 230B of the Act);
- (b) to impose conditions on the entity's registration (sections 22 and 28B of the Act);
- (c) to investigate life insurance business of a body corporate that is a life company, or business of a body corporate that is a registered NOHC (section 137 of the Act); and
- (d) to revoke a life company's registration under section 21 if APRA is satisfied that the company has no liabilities in respect of life insurance business carried on by it in Australia (section 26 of the Act) or to revoke a registered NOHC's registration under section 28A (section 28C of the Act).

A decision of APRA to give a direction or impose a condition is subject to merits review under section 236 of the Act. Before exercising such a power, APRA will give an affected body corporate an opportunity to comment on the whether the exercise is warranted or not. Revocation of a life company's registration or a life NOHC's registration is subject to merits review (section 236 of the Act).

Adjust and exclude discretion

The new LPS 112 gives APRA the discretion to adjust or exclude a specific requirement in the prudential standard (paragraph 6). The power to include such a discretion is provided for under subsection 230A(4) of the Act.

APRA may exercise this power when it is satisfied that the adjustment or exclusion of a specific requirement will better support APRA in meeting its objectives. For example, the adjustment or exclusion may be necessary to obtain a better prudential outcome than would be the case if the prudential requirement were applied unaltered. A tailored approach gives APRA greater flexibility to ensure that the prudential requirements are fit for purpose and protect the interests of policyholders. APRA will also take into account other considerations, such as efficiency, competition, contestability, competitive neutrality and regulatory burden.

The exercise of APRA's powers is governed by a robust decision-making framework. This framework supports APRA in fulfilling its mandate by limiting decision-making to those APRA officers with the appropriate experience and skill to exercise prudent judgement.

4. Documents incorporated by reference

Under paragraph 14(1)(a) of the *Legislation Act 2003*, the prudential 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 230A(1) of the Act;
- Reporting Standards determined by APRA under subsection 13(1) of the *Financial Sector (Collection of Data) Act 2001*;
- 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).

5. Consultation

APRA undertook two separate rounds of public consultation on proposed changes to its capital settings for longevity products (including annuities).

In June 2025, APRA released a consultation paper inviting industry feedback on certain proposed changes to the life insurance capital framework for longevity products. In response, APRA received 11 submissions from entities and industry bodies. APRA also undertook additional engagements with several stakeholders. Submissions were generally supportive of APRA's direction and included a range of suggestions to refine the proposal. The main suggestion was that the proposed capital benefit should be better aligned with the level of risk controls proposed. This feedback was accepted and informed the development of draft revised prudential standards.

In October 2025, APRA undertook a second round of consultation inviting further feedback on APRA's refined proposal, including a draft version of the new LPS 112. APRA received nine submissions, primarily from entities and industry bodies. Industry feedback strongly supported the reforms, with it being noted that the changes represent a significant improvement to the current framework by reducing procyclical risks to life insurers' capital positions. Stakeholders noted APRA's reforms represent an important step towards developing Australia's retirement income market by promoting innovation and expanding options for retirees to manage longevity risk. Respondents indicated that they largely expect the reforms to improve capital efficiency and stimulate greater market participation.

While overall feedback was positive, many submissions suggested some further refinements to specific parameters of the proposed 'advanced illiquidity premium' (AILP) calculation, notably in relation to the proposed floor for the risk allowance and treatment of the AILP in the credit spread stress charge under *Prudential Standard LPS 114 Capital Adequacy: Asset Risk Charge*. Mixed views were received in relation to proposed restrictions on assets backing longevity products, ranging from recommending the removal of restrictions to advocating for

greater flexibility and higher asset limits. APRA acknowledged the feedback received but determined that the proposed settings for the AILP remain sound and strike the right balance in providing capital efficiency in return for appropriate risk controls.

In March 2026, APRA released a response paper finalising the changes to its capital settings for longevity products, including the new LPS 112. All relevant consultations and non-confidential submissions are available on APRA's website.

APRA is satisfied that the consultation undertaken was appropriate and reasonably practicable.

6. Impact Analysis

The Office of Impact Analysis confirmed that a Regulation Impact Statement was not required.

7. 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 included in Attachment B to this Explanatory Statement.

ATTACHMENT A

Description of key provisions of the new LPS 112

1. Capital base of a life company

The capital base must be assessed for the life company as a whole and for each of its funds. Paragraphs 14 to 50 set out the requirements for the life company as a whole.

The capital base of a life company consists of Common Equity Tier 1 (CET1) Capital, Additional Tier 1 (AT1) Capital, paid-up mutual equity interests issued by mutually-owned life companies and Tier 2 (T2) Capital. Attachment A lists the criteria for an instrument to be classified as paid-up ordinary shares in CET1 Capital. Attachment C sets out the criteria for an instrument to be classified as AT1 Capital. Attachment D outlines the criteria for an instrument to be included as T2 Capital. Attachment G sets out the criteria for an instrument issued by a mutually-owned life company to be classified as a mutual equity interest.

2. Regulatory adjustments to CET1 Capital

Attachment B sets out regulatory adjustments required to be made to ensure the capital base is adequate to support the activities of the life company.

A life company must deduct the liability adjustment. Liability adjustments are outlined in Attachment B paragraphs 25-26, requiring insurance liabilities in the statutory accounts to be replaced with adjusted policy liabilities when determining the capital base. The method of determining the adjusted policy liabilities is specified in Attachment F.

3. Capital base of a statutory fund or general fund

The capital base requirements for statutory funds are specified in paragraphs 51-54. The requirements for general funds are specified in paragraphs 55-57.

4. Minimum requirements regarding size and composition of a capital base

Paragraphs 15, 53, and 56-57 set out the minimum requirements regarding size and composition of a capital base for a life company, statutory fund and general fund respectively.

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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This 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 this instrument is to revoke *Prudential Standard LPS 112 Capital Adequacy: Measurement of Capital* (LPS 112) made under *Life Insurance (prudential standard) determination No. 1 of 2024* and replace it with a new version of LPS 112 to incorporate certain changes arising out of APRA's review of its capital framework for longevity products.

LPS 112 is designed to ensure life companies remain financially resilient by maintaining sufficient capital against the risks associated with their activities.

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.

Conclusion

Accordingly, in APRA's assessment, this legislative instrument is compatible with human rights as it does not raise any human rights issues.