



## **Prudential Standard APS 120**

### **Funds Management and Securitisation**

#### **Objective and key requirements of this Prudential Standard**

This Prudential Standard aims to ensure that authorised deposit-taking institutions adopt prudent practices to manage the risks arising out of their involvement in funds management and securitisation activities, and to ensure that appropriate capital is held against the risks involved.

## Authority and application

1. This Prudential Standard, made under section 11AF of the *Banking Act 1959* (**the Act**), applies to all authorised deposit-taking institutions (**ADIs**) authorised under the Act.
2. *Guidance Notes AGN 120.1 Disclosure and Separation (AGN 120.1)*, *AGN 120.2 Credit Enhancement (AGN 120.2)*, *AGN 120.3 Purchase and Supply of Assets (including Securities Issued by Special Purpose Vehicles) (AGN 120.3)*, *AGN 120.4 Liquidity, Underwriting and Lending Facilities (AGN 120.4)* and *AGN 120.5 Servicing, Managing and Treasury Dealings (AGN 120.5)* form part of this Prudential Standard.
3. This Prudential Standard does not apply to foreign ADIs,<sup>1</sup> except for the provisions relating to disclosure and separation. In their conduct of funds management or securitisation activities in Australia, foreign ADIs should have regard to all the disclosure and separation requirements.

## Overview

4. Funds management encompasses the provision of investment and related services for the management of investors' funds. Securitisation involves the pooling of assets, or interests in assets, in a special purpose vehicle (**SPV**), which is funded by the issue of securities.
5. ADIs<sup>2</sup> can incur financial, credit, operational and legal risks arising from the obligations associated with their funds management and securitisation activities. Involvement in these activities can also yield moral risk - the possibility that an ADI will feel a moral obligation or a commercial need to support a funds management or securitisation scheme, or the investors involved in such schemes, beyond any explicit legal obligation to do so.
6. It is the responsibility of the Board and management of an ADI to put in place clear strategies and policies to govern an ADI's involvement in funds management and securitisation activities. These should incorporate appropriate management systems to identify, measure and control risks, including liquidity risks and potential conflicts of interest, arising from the ADI's involvement in these activities.

## ADI's involvement in funds management & securitisation activities

7. An ADI's role in a funds management or securitisation scheme can range from the establishment and sponsorship of the whole scheme to the provision of a single facility or service to a scheme sponsored by independent parties. Regulatory treatment, including for capital and disclosure, will vary depending on the risks that the ADI has to bear.

---

<sup>1</sup> For the purposes of this Prudential Standard, foreign ADI has the same interpretation as in Division 1B of the *Banking Act 1959*.

<sup>2</sup> For the purpose of this standard and the associated guidance notes, reference to "ADI" or "ADIs" includes an ADI and its subsidiaries unless otherwise stated.

8. Where the provision of facilities or services meet disclosure, separation and arm's length criteria as listed in AGN 120.1, AGN 120.2, AGN 120.3, AGN 120.4 and AGN 120.5, they will be subject to capital requirements in accordance with *Prudential Standard APS 112 Capital Adequacy: Credit Risk*. Otherwise, an ADI may be required to hold capital, on a solo and consolidated group basis, against the full value of securities<sup>3</sup> issued by the SPV<sup>4</sup> with which it is involved.
9. Where the totality of an ADI's involvement in funds management and securitisation suggests that the overall level and/or concentration of risks has become excessive relative to its capital, APRA may require the ADI to maintain a buffer above the minimum capital ratio. In extreme circumstances, where there is evidence of misleading investors or incorrect perception of ADI support, such that the additional risks would not be adequately addressed by holding additional capital, an ADI may be precluded from continuing to undertake funds management and securitisation activities.
10. This Prudential Standard and its associated Guidance Notes apply to all forms of funds management and securitisation activities undertaken by ADIs in both the retail and wholesale markets. It also covers securitisation arrangements where the exposures do not cross an ADI's balance sheet. The provisions should also be considered in any asset sales undertaken by an ADI where the ADI provides support services or other facilities to the buyer.
11. An ADI should consult APRA in advance of undertaking any new funds management or securitisation schemes, except where the structure involved has been previously provided to APRA by the ADI.

## Disclosure

12. A key feature of funds management and securitisation schemes is that the payment of earnings and the return of capital to investors hinge on the cash flows from the underlying assets in which their funds are invested. Investors are exposed to investment risk, which may not be clear when investors are dealing with an ADI. To eliminate confusion, an ADI's involvement in such schemes should be accompanied by clear disclosure that the investment in the schemes does not represent deposit or other liabilities of the ADI involved. Any recourse to the ADI for repayment of principal and/or interest will require appropriate capital support.

## Separation

13. To achieve separation, an ADI must deal with a SPV and/or its investors at arm's length and on market terms and conditions. An ADI's undertaking in any funds management or securitisation scheme should be stand-alone, with the

---

<sup>3</sup> Securities, in relation to funds management or securitisation schemes, include debt instruments, shares, investment units, "partnership" interests, investment type products, and any other form of beneficial interest.

<sup>4</sup> A SPV is an entity which holds assets and issues securities to (or receives funds from) investors in order to facilitate the management of investors' funds and/or the securitisation of assets.

extent of the ADI's obligations set out in legal documentation. Where this does not occur, the ADI will need to hold capital against the full value of securities on issue.

### **Clean sale**

14. An ADI will be relieved of the need to hold capital in support of assets sold to SPVs only where the sale of the assets is clean and final (refer AGN 120.3). An ADI may incur risks or returns in respect of the assets sold as a result of the ADI providing facilities covered by this Prudential Standard or the associated Guidance Notes. Should the ADI retain any obligation, risk or interest relating to the assets sold other than arising from such facilities, the assets must be treated as if they were still on the ADI's balance sheet. In supplying assets to SPVs, ADIs should ensure that it will not lead to deterioration in the average quality of assets remaining on its balance sheet.