Response to Submissions

Basel III disclosure requirements: composition of capital and remuneration

June 2013
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In April 2013, the Australian Prudential Regulation Authority (APRA) released a discussion paper, Basel III disclosure requirements: composition of capital and remuneration, outlining its proposals for enhanced public disclosure by authorised deposit-taking institutions (ADIs) in Australia. These proposals give effect to measures introduced by the Basel Committee on Banking Supervision (Basel Committee) to address deficiencies identified during the global financial crisis in the information banks disclose publicly. The composition of capital and remuneration disclosure measures are set out in the Basel Committee’s Composition of capital disclosure requirements (June 2012) and Pillar 3 disclosure requirements for remuneration (July 2011), respectively. Concurrent with the release of the April 2013 discussion paper, APRA also released for consultation a draft Prudential Standard APS 330 Public Disclosure (draft APS 330).

This response paper addresses the submissions received on the April 2013 discussion paper. Accompanying it is the final version of APS 330, which will come into effect on 30 June 2013.

This response paper and the final prudential standard are available on APRA’s website at www.apra.gov.au/adi/Pages/adi-consultation-packages.aspx.
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## Glossary

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Executive summary

In December 2010, in response to the global financial crisis, the Basel Committee released a package of reforms (Basel III)\(^1\) to raise the level and quality of regulatory capital in the global banking system. Included in this package were proposals for expanded disclosure measures that are intended to improve the transparency of regulatory capital and to enhance market discipline. Final details of these measures were released in June 2012\(^2\). Also in response to the crisis, the Basel Committee released its disclosure framework for remuneration in July 2011\(^3\). APRA is a member of the Basel Committee and fully supports the implementation of these disclosure requirements.

In April 2013, APRA issued a consultation package outlining its proposals to implement these Basel III capital and remuneration disclosure measures in Australia\(^4\). APRA received eight submissions on the consultation package and subsequently met with industry representatives to discuss its proposals.

Submissions raised three main issues as well as a number of technical queries. The main issues were the scope of application of the disclosure requirements, the implementation date, and the international comparability of capital ratios.

Several submissions questioned the relevance of the capital and remuneration disclosures to mutually owned ADIs and requested that APRA consider whether a more streamlined form of disclosure for these ADIs could achieve the same outcome. However, APRA is not persuaded that the owners of mutual ADIs should have access to a lower standard of disclosure than the owners of other ADIs. In addition, the range of parties interested in ADI disclosure is potentially broad, regardless of an ADI’s ownership structure. Given that ADIs need only complete the various disclosure templates to the extent applicable to them, APRA does not intend to create a separate template for any subset of ADIs.

Several submissions raised concerns about the proposed implementation date of 30 June 2013, particularly ADIs with 30 June reporting dates that may need to commence their preparatory work before APS 330 is finalised. The implementation date is a globally agreed one and announced some time ago by the Basel Committee, and APRA has consistently advised industry of its intention to implement the disclosure measures in full from that date. Accordingly, APRA does not propose to change the implementation date. However, it will accept entities reporting the new Pillar 3 disclosures on capital and remuneration on a ‘best endeavours’ basis for the June 2013 reporting date only.

In order to facilitate the international comparability of regulatory capital ratios, APRA proposed to provide an addendum to the common disclosure template that would compare capital ratios under APRA’s requirements with capital ratios under Basel III; differences would mainly reflect the exercise of national discretions available within the Basel III framework. APRA did not propose to include differences arising from the measurement of risk-weighted assets, an issue under review by the Basel Committee. Several submissions considered that the addendum could be potentially misleading. In response, APRA has decided to remove the addendum and await the conclusion of the Basel Committee’s work before considering additional disclosures in this area. However, ADIs may disclose further information on regulatory capital ratios if they wish.

APRA’s full response to submissions regarding the capital disclosure requirements are outlined in Chapter 1, while Chapter 2 addresses submissions on the disclosure requirements for remuneration. Attachment A addresses a number of technical queries on capital disclosures.

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1 The revised June 2011 text is at [http://www.bis.org/publ/bcbs189.htm](http://www.bis.org/publ/bcbs189.htm)
2 [http://www.bis.org/publ/bcbs221.htm](http://www.bis.org/publ/bcbs221.htm)
3 [www.bis.org/publ/bcbs197.pdf](http://www.bis.org/publ/bcbs197.pdf)
Chapter 1 — Disclosure requirements for composition of capital

APRA’s April 2013 consultation package consisted of a discussion paper, Basel III disclosure requirements: composition of capital and remuneration and a draft prudential standard, Prudential Standard APS 330 Public Disclosure (draft APS 330). APRA’s proposals on capital disclosure were intended to give effect to the Basel Committee requirements set out in its 2012 publication, Composition of capital disclosure requirements.

1.1 Scope of application

APRA proposed that, in parallel with its application of the Basel III capital reforms, the capital disclosure requirements would apply to all locally incorporated ADIs, other than providers of purchased payment facilities (PPF providers). For some requirements, this would extend the current scope of APS 330 to include ADIs using the ‘standardised’ Basel II approaches for measuring credit and operational risk.

Comments received

Several submissions questioned the relevance of the capital (and remuneration) disclosures to mutually owned ADIs. These submissions requested that APRA give further consideration to whether these disclosures were required and, if so, whether a more streamlined form of disclosure could achieve the same outcome. Submissions noted that the current APS 330 (implementing the Basel II capital framework) requires less complex disclosure for ADIs using the standardised Basel II approaches.

APRA’s response

APRA is not persuaded that the owners of mutual ADIs should have access to a lower standard of disclosure than the owners of other ADIs. In addition, the range of parties interested in ADI disclosure is potentially broad, regardless of an ADI’s ownership structure. APRA notes that the intention of the Basel III capital disclosures is to facilitate comparison between ADIs both within and across jurisdictions. APRA considers that this objective applies to all ADIs, regardless of ownership structure.

The current version of APS 330 does distinguish between ADIs on the basis of whether they have been approved to use the Basel II advanced approaches for measuring credit risk and operational risk, or are on the Basel II standardised approaches. This distinction is not relevant for the Basel III requirements, which are broader in scope and in Australia are applicable to all ADIs. In any event, ADIs need only complete the various templates to the extent applicable to them. Consequently, APRA does not propose to alter the scope of application of the capital disclosure requirements.

1.2 Implementation date

APRA proposed that the capital disclosure requirements come into effect from reporting dates on or after 30 June 2013.

Comments received

Several submissions queried the proposed implementation date of 30 June 2013, particularly those ADIs with 30 June reporting dates. The concern was that the new requirements necessitate changes to governance and operational processes, which take time, and that work will need to commence before the final APS 330 is released.

APRA’s response

APRA recognises this concern but notes that draft APS 330 closely mirrors the Basel Committee’s disclosure measures and APRA has been advising industry since 2009 of its intention to implement the measures in full. Furthermore, the Basel Committee’s rules text for the capital disclosure measures, released in June 2012, clearly detailed an implementation date of 30 June 2013.

Accordingly, APRA does not propose to change the 30 June 2013 implementation date for the capital disclosure requirements. However, APRA will accept entities reporting the new Pillar 3 disclosures on a ‘best endeavours’ basis for the June 2013 reporting period only. ‘Best endeavours’ will, at a minimum, require reporting consistent with draft APS 330 released in April 2013. Disclosures for subsequent reporting dates must fully comply with the final APS 330.
Draft APS 330 stated that the disclosures required in the ‘main features’ template (Attachment B) ‘must be published continuously commencing on the date when this Prudential Standard comes into effect.’ This wording implies that these disclosures will need to be made by all ADIs from 30 June 2013, irrespective of the balance date of the ADI. This was not APRA’s intention. APRA clarifies that an ADI must disclose the main features template for each capital instrument included in its regulatory capital commencing from its first statutory reporting date on or after 30 June 2013, and thereafter on a continuous basis.

1.3 Audit requirements

APRA proposed that an ADI must include certain disclosures in its financial statements or, at a minimum, the financial statements must include a direct link to the completed disclosures placed in the Regulatory Disclosures section on the ADI’s website.

Comments received

Several submissions sought clarification on the potential audit requirements for the APS 330 capital disclosures. The concern was that requiring a link to disclosures in an ADI’s financial statements could trigger a requirement for those disclosures to be audited to the same standard of assurance as the balance sheet, profit and loss and cash flow statement.

APRA’s response

Unless specifically required by APRA, disclosures under APS 330 are not subject to external audit. However, such disclosures must be consistent with information that has been subject to review by an external auditor and that is published elsewhere, or has been already supplied to APRA. Consequently, APRA requires that the relevant prudential disclosures (or link thereto) be included in the ADI’s financial report, director’s report or other information accompanying the ADI’s financial report.

1.4 Common disclosure template — addendum

In response to industry concerns about the international comparability of regulatory capital ratios, APRA proposed to provide an addendum to the common disclosure template that would compare capital ratios under APRA’s requirements (after applying national discretions) and under Basel III rules (not applying national discretions). The addendum focused on the numerator of the capital ratio and was intended to identify differences in regulatory capital ratios due to the different exercise of national discretions available under Basel III.

Comments received

Several submissions objected to the addendum on the basis that by not focussing as well on the denominator — the measurement of risk-weighted assets — the regulatory capital ratios could be misleading. Submissions recommended that APRA either:

• replace the proposed addendum with internationally harmonised capital ratios that allow for differences from the full Basel capital framework in both the numerator (definition of capital) and the denominator (risk-weighted assets); or
• remove the addendum until fully harmonised regulatory capital ratios can be developed.

APRA’s response

The Basel Committee is currently undertaking a substantial exercise on the measurement of risk-weighted assets, aimed at ensuring consistent implementation of the full Basel capital framework, including Basel II and Basel II.5, so as to maintain market confidence in regulatory ratios and provide a level playing field. The exercise includes hypothetical test portfolio analysis designed to identify areas and sources of material inconsistencies, on both the banking book and the trading book, across banks and jurisdictions. APRA proposes to await the conclusion of this work before considering additional disclosures in this area.

Accordingly, APRA has decided to remove the addendum at this point. However, ADIs are free to disclose further information on regulatory capital ratios if they wish. APRA will continue to work with industry and within the Basel Committee on the international comparability of capital ratios.

1.5 Common disclosure template — institution-specific buffers

Row 64 of the common disclosure template requires ADIs to input institution-specific buffer requirements (minimum CET1 requirement plus capital conservation buffer plus countercyclical capital buffer requirements plus any globally systemic banking institutions (G-SIB) requirement (currently not applicable in Australia), expressed as a percentage of risk-weighted assets).

Comments received

Submissions enquired if ADIs need to disclose institution-specific capital conservation buffers or whether such buffers should be confidential in the same manner as prudential capital requirements (PCRs).

APRA’s response

It is not APRA’s intention that an ADI disclose any information that may indirectly lead to the disclosure of its PCR. Accordingly, and to provide further clarity, APRA has amended row 64 in the common disclosure template and the accompanying guidance. An ADI must report the minimum Basel III CET1 requirement of 4.5 per cent and 2.5 per cent for the capital conservation buffer. If a countercyclical capital buffer were to apply, an ADI will need to disclose that buffer.

1.6 Reconciliation requirements

1.6.1 List of entities

As part of the reconciliation requirements, APRA proposed that an ADI must disclose the list of legal entities that are included within the accounting scope of consolidation but excluded from the regulatory scope of consolidation, and vice-versa.

Comments received

Several submissions sought clarification on whether only material entities or company groups need to be disclosed.

APRA’s response

Based on concerns flowing from the global financial crisis about the impact of entities excluded from regulatory capital measures, and to enable a full recognition of the potential impact of such entities, the Basel Committee requires a full list of entities that are not included in the regulatory scope of consolidation but are within the accounting scope of consolidation, and vice-versa. Full disclosure enables better comparison between ADIs and seeks to minimise the risk of any inadvertent exclusion of non-consolidated entities when disclosures are made. Against this background, APRA sees no need to change its requirement that full disclosure of all entities must be made.

1.6.2 Reconciliation process — prudential items

The reconciliation process is expected to reconcile the balance sheet with the common disclosure template.

Comments received

Submissions noted that the reconciliation process assumes all components of the capital calculations can be derived directly from the balance sheet. They indicated, however, that this is not the case for certain specific prudential items such as expected loss, which contribute towards the deduction relating to the shortfall of provisions. It was recommended that where capital calculations cannot be derived directly from the balance sheet, guidance should be provided on how these items are to be reported.

APRA’s response

Where items cannot be reconciled with the balance sheet, this should be simply noted in the reconciliation and the source of the information cited. This will point out that the capital positions can be aligned, but not determined fully from published balance sheet information.
1.6.3 Reconciliation process — coverage

Comments received
Submissions argued that any reconciliation between financial statements and the capital calculations should be limited to the adjustments required to shareholders equity to produce CET1. The level of detail in the proposed disclosure was claimed to be excessive and could overwhelm users of information.

APRA’s response
APRA confirms that the reconciliation process relates not just to CET1 but also to measures of Tier 1 and Total Capital. The process encompasses not only capital components forming part of these capital measures but also the sources of any adjustments to these capital measures. Consequently, APRA does not propose to limit the reconciliation requirements.

1.7 Timing of disclosure

Draft APS 330 proposed that an ADI’s financial statements must include the new capital disclosures in full or must include a direct link to the completed capital disclosures, located on the ADI’s website.

Comments received
Submissions queried whether the ‘direct link’ option means that, where an ADI chooses to disclose the capital disclosures in a separate APS 330 document (as is the current common practice in Australia), the APS 330 document will need to be published on the same day as the financial statements. The current practice of releasing the APS 330 document within two weeks of the financial statements has, it was claimed, allowed a staging of governance and assurance processes during a very busy period for all ADIs, which submissions argued results in a higher quality document.

APRA’s response
APRA does not propose to amend the proposed requirement that disclosures be made concurrently with an ADI’s normal statutory financial reporting period. Consequently, an ADI must make the appropriate capital disclosures at the same time as the lodgement of its financial statements.

In addition, APRA has aligned the timing of disclosures under Attachment C and D of APS 330. In the case of Attachment C, quarterly disclosures coinciding with the lodgement of financial reports under the Corporations Act 2001 (Corporations Act) are to be made concurrently with the financial statements. Disclosures in the quarter not coinciding with the lodgement of financial reports are to be made within 40 days after the end of the reporting period. Disclosures under Attachment D are to be published concurrently with the lodgement of financial reports.
Chapter 2 — Disclosure requirements for remuneration

APRA’s April 2013 consultation package also included its proposals for implementing the qualitative and quantitative disclosure requirements for remuneration set out in the Basel Committee’s 2011 document, Pillar 3 Disclosure Requirements for Remuneration.

2.1 Scope of application

APRA proposed that the disclosure requirements for remuneration apply to all locally incorporated ADIs, other than PPF providers and specialist credit card institutions (SCCIs).

Comments received

Some submissions queried whether the proposed scope of application is consistent with APRA’s commitment, set out in a letter to industry in October 2011, to adopt a proportionate approach to remuneration disclosure, taking account of an institution’s nature, size and complexity. They noted that disclosure requirements under the Corporations Act 2001 (Corporations Act) are designed primarily to inform shareholders of information about an institution’s remuneration, and argued that such information is irrelevant for ADIs that are member-owned. The submissions sought an exemption from the remuneration disclosures for mutually owned ADIs or, alternatively, a simplified reporting requirement.

APRA’s response

The proposed measures are designed to improve the transparency of an ADI’s remuneration for market participants, including owners, regardless of whether owners are holders of ordinary shares or members of a mutually owned ADI. APRA sees no reason therefore not to require full disclosure of remuneration by all ADIs.

2.2 Implementation date, frequency, timing and location

2.2.1 Implementation date

Draft APS 330 proposed that, as with the capital disclosure requirements, ADIs make remuneration disclosures from their first balance sheet date on or after 30 June 2013.

APRA’s response

Following the release of the Basel Committee’s requirements, APRA wrote to all ADIs in October 2011 advising of its intention to incorporate the remuneration disclosure requirements as part of ADI Pillar 3 reporting requirements. In that letter, APRA encouraged all locally incorporated ADIs to commence reporting on their remuneration practices in a manner consistent with the Basel Committee requirements as soon as practicable. Furthermore, the new measures largely require public disclosure about remuneration policies and procedures that an ADI is required to have in place in accordance with Prudential Standard CPS 510 Governance (CPS 510). Consequently, APRA does not consider that it is appropriate to amend the implementation date.

2.2.2 Timing of disclosures

Draft APS 330 proposed that an ADI publish its remuneration disclosures concurrently with the publication of its audited financial statements.

Comments received

Several ADIs asked APRA to relax this requirement, stating that final positions on remuneration, particularly for non-key management personnel that might be captured under APS 330, were often not finalised prior to release of financial statements. Various alternative timeframes were proposed that would delay the publication of the remuneration disclosures until after the publication of financial statements.

APRA’s response

In view of these submissions, APRA has reconsidered its position and proposes to allow the publication of remuneration disclosures no later than three months from the lodgement of an ADI’s annual financial report.
2.2.3 Location

Draft APS 330 proposed that an ADI must include a Regulatory Disclosures section on its website. The section must include its prudential disclosures, either in full or through links to other websites. An ADI that does not have a website must obtain APRA's approval for alternative publication arrangements.

Comments received
Clarification was sought as to whether an ADI with a parent company that relies on the parent’s policy, procedures and governance arrangements for remuneration must also meet the disclosure requirements on its own website. It was also queried whether making reference and providing a link to the parent’s Corporations Act remuneration report in its Pillar 3 disclosures would satisfy the requirements of APS 330.

APRA’s response
Under CPS 510, the Board of an ADI must be satisfied that all governance arrangements, policies and procedures, including those relating to remuneration, are appropriate to the ADI, including those emanating from the corporate group.

APRA confirms that an ADI, regardless of its ownership, must have a Regulatory Disclosures section on its website that either includes the remuneration disclosures as they relate to the ADI, or provides a link to those disclosures, which may be included in a document published by its parent. However, APRA expects that any disclosures made by the parent will clearly identify the disclosures under APS 330 as they relate to the ADI. As stated in the April discussion paper, APS 330 remuneration disclosures in a Corporations Act remuneration report must be clearly distinguished from those made under that Act.

2.3 Confidentiality and privacy

Attachment E of draft APS 330 requires ADIs to make various quantitative and qualitative remuneration disclosures.

Comments received
Several submissions were concerned that disclosing information that related only to a small number of individuals could potentially breach privacy/confidentiality obligations (for instance, where only one individual is subject to clawback). It was suggested that a materiality threshold of five individuals should apply before disclosure is required or that APRA consider amending the disclosure requirements or limiting the application so that sensitive or confidential information would not be published.

APRA’s response
APRA notes that several ADIs are already disclosing aggregate remuneration details on key management personnel as required under the Corporations Act. Notwithstanding this, APS 330 has been amended to allow an ADI to disclose more general information about remuneration where disclosures of certain items of information may prejudice the position of the ADI, or any other person, by making public information that is proprietary, confidential or personal in nature. APRA may direct an ADI to expand its remuneration disclosures if, in APRA’s view, the disclosures are not adequate.

2.4 Other queries

2.4.1 Senior managers and material risk-takers

For the purposes of the quantitative remuneration disclosures in Tables 18 and 18A, draft APS 330 defined ‘senior managers’ and ‘material risk-takers’ by reference to a sub-set of the personnel to be included in an ADI’s remuneration policy under CPS 510.
Comments received
Some submissions queried whether the draft APS 330 definitions aligned with CPS 510. They further queried whether the qualitative disclosures in Attachment E are restricted to senior managers and material risk-takers.

APRA’s response
APRA confirms that the definitions of senior manager and material risk-taker align with CPS 510. Draft APS 330 had reproduced verbatim the text of CPS 510. However, in light of submissions, APRA has simplified APS 330 to refer only to the relevant provisions of CPS 510. APRA has also changed the reference to ‘employees’ in Attachment E to ‘persons’ to more fully align with the CPS 510 definitions.

APRA confirms that the qualitative information to be disclosed under APS 330 relates to all persons captured under an ADI’s remuneration policy in accordance with CPS 510, which is broader than senior managers and material risk-takers.

2.4.2 Quantitative disclosures
Table 18(h) includes a number of quantitative disclosures relating to employees receiving variable remuneration awards (bonuses, sign-on awards, severance payments) during the financial year.

Comments received
Submissions sought clarification as to whether these amounts should capture remuneration awarded in respect of performance for the financial year, or remuneration paid during the financial year (but which may relate to performance in other year(s)).

Clarification was also sought about the ambit of severance payments e.g. whether to include unvested benefits released on termination.

APRA’s response
It is APRA’s view that the publication of remuneration information assists market participants to assess the award of remuneration of employees vis-à-vis their performance for the year. As a consequence, ADIs should align the reporting of remuneration with the financial year in which the services were rendered, irrespective of whether it was vested or unvested or when any consequential cash distributions might be affected.

2.4.3 Terminology
Comments received
Submissions queried APRA’s proposed requirement that ADIs disclose their ‘criteria’ for determining individual remuneration, indicating that this suggested a set list of factors. It was proposed that the word ‘approach’ more properly represented how remuneration decisions are made.

The reference to ‘severance payments’ was also queried.

APRA’s response
APRA does not support departing from the Basel rules text, which employs ‘criteria’. APRA expects that the description ADIs use to meet this requirement will demonstrate how remuneration decisions are made.

APRA accepts that ‘severance payments’ are known as ‘termination payments’ under Australian law and has amended APS 330 accordingly.
Attachment A – Technical queries relating to capital disclosure

In response to technical queries on the capital disclosures, APRA provides the following clarifications.

- The splitting of the greater than 15 per cent threshold required by lines 23 through 25 is to be done on a pro rata basis.
- Rows 26(d) and 26(e) in the common disclosure template must include the additional amounts to be deducted as a result of APRA’s regulatory adjustments in respect of equity investments in financial institutions and deferred tax assets.
- The starting point for compilation of regulatory capital in the common disclosure template is the consolidated Level 2 position. The common disclosure template is reported on a Level 2 basis where non-consolidated entities are to be treated as not forming part of the group. The retained earnings figure is to be adjusted for the retained earnings and other reserves of deconsolidated entities such as insurance and funds management entities.
- Cash flow reserves may be generated by entities in the Level 2 group and so form part of items required to be disclosed for the Level 2 group; however, an insurance entity is not in the Level 2 group. For entities outside of the Level 2 group, only earnings actually transferred to Level 2 group members (e.g. by paid dividend) may be counted in the earnings reported for the Level 2 group.
- APRA does not expect the provision of comparatives in the capital disclosures (comparatives are specified for Attachments C and D and remuneration disclosures). However, the capital disclosures are to be archived for 12 months.
- ADIs should not amend regulatory reporting in the APRA forms to be in line with the common disclosure template. ADIs must continue to report to APRA on the basis of Reporting Standard ARS 110 Capital Adequacy.
- Where an item is not relevant, ‘not applicable’ should be utilised; ‘0’ should be used when the value of that item is zero.
- ADIs must not insert any additional rows in the common disclosure template.

Main features template

- ADIs must use the main features template but may add explanatory notes to allow for any unique features of instruments.
- ADIs must provide full disclosure of each instrument on an individual basis. Disclosures for instruments that have the same terms and conditions, e.g. Tier 2 subordinated debt, cannot be aggregated.
- Common shares must also be included in the main features template. The intent is to ensure complete disclosure across entities and jurisdictions to avoid the potential for misreporting of components of capital, such as through creation of new forms of capital instruments.
- APS 330 Attachment B Table 2, item 8 – if a capital instrument has to be discounted for tax or other effects impacting on its value, the item must be reported at the discounted value. For example, if an Additional Tier 1 instrument only counts as 80 instead of 100 on conversion under a non-viability event because of tax effects, item 8 will show the capital value of the instrument as 80, not 100.
- APS 330 Attachment B Table 2, item 35 – where the issue documentation provides for ranking on conversion or partial conversion in a loss absorption or non-viability event, this may also be included in item 35.
- APS 330 Attachment B Table 2, item 15 – where the instruments under transition allow for calls based on take-over events, this may be included in item 15.