



7 December 2020

TO: ALL AUTHORISED DEPOSIT-TAKING INSTITUTIONS

SCRUTINY OF SECURITISATION PRACTICES

The Australian Prudential Regulation Authority (APRA) has recently identified that some authorised deposit-taking institutions (ADIs) repurchased residential mortgage loans that were subject to repayment deferral from their securitisations. In APRA's view, this represents implicit support, which is inconsistent with Prudential Standard APS 120 Securitisation (APS 120), paragraph 13(b).¹ APS 120 requires ADIs to be clearly separate from their securitisations and to permanently (except in limited pre-defined circumstances) transfer credit risk to the securitisation investors.

APS 120 only allows ADIs to repurchase mortgages from their securitisations under limited circumstances and if the borrower is in good standing. The intent of APS 120 is that mortgages are not repurchased by ADIs if the borrower is in hardship or the loan is of lower quality, as this would undermine the principle of a clear transfer of credit risk that is at the heart of the regulatory treatment of securitisation.

APRA has required the ADIs that it considers to have provided implicit support to publicly disclose their repurchases as part of upcoming Pillar 3 reporting requirements. They will also be required to have a third party review their program's APS 120 compliance and mitigate the findings prior to further securitisation issuance.

APRA also identified other issues in relation to compliance with APS 120 within these ADIs. Based on these findings and engagement with industry stakeholders, APRA believes it is necessary to conduct a program of securitisation thematic reviews. This has commenced and will continue into 2021.

Depending on the findings, the reviews may be expanded further. Identification of non-compliance with APS 120 may result in the ADI being required to publicly disclose their non-compliance and/or a requirement to hold additional regulatory capital.

Additional consequences for non-compliance with APS 120 may also include the need for engagement of an APRA-approved independent third party to review the ADI's compliance with the prudential standard and APRA pre-approval of further securitisation issuance.

In advance of these APRA reviews, APRA recommends ADIs ensure they comply with the letter and intent of APS 120 and ensure controls and procedures are in place to maintain compliance. This applies to the documentation and ongoing management of the securitisation.

Deficiencies already identified by APRA as part of its thematic reviews include:

¹ This paragraph states that ADIs must "not provide, or knowingly create or encourage a perception that it will provide, implicit support for a securitisation".

- little or no procedures or controls to challenge or provide oversight of ongoing securitisation operations, such as approving repurchases;
- requirements for ADIs to repurchase loans from their securitisations under certain circumstances, in breach of APS 120 paragraph 18; and
- considering capitalising interest to be a further advance and insufficiently considering the provision of implicit support and the guidance in Prudential Practice Guide APG 120 Securitisation for the purposes of APS 120, Attachment A, paragraph 6.

Self-identification and timely reporting by ADIs to APRA of non-compliance will be favourably considered by APRA when determining the appropriate actions.

If you have any questions, please contact your Supervisor.

Yours sincerely,

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