5 July 2019

Ms Heidi Richards
General Manager
Policy Development
Policy and Advice Division
Australian Prudential Regulation Authority

By email: ADIpolicy@apra.gov.au

Dear Ms Richards

APS 220 Credit Risk Management Consultation

Thank you for the opportunity to make a submission on the proposed revision to the Prudential Standard APS 220 Credit Risk Management Consultation (APS 220).

The ABA welcomes the timely review of APS 220 to incorporate the new developments in credit risk management practices including the new accounting standards and the Basel Committee supervisory guidance on sound credit risk practices. The ABA agrees that effective management of credit risk is a critical component of a comprehensive approach to risk management and essential to the long-term viability of any ADI. However, regulatory requirements should not create competitive impediments between ADIs and non-ADIs.

This submission considers the following topics:

1. Credit Risk management framework
2. Asset Classification
3. Provisioning
4. Supervisory limits
5. Collateral and security valuation (Attachment A)
6. Competition impacts

Each of these is considered below.

1. Credit risk management framework

1.1 Valuations

The ABA is concerned that APS220 as drafted with regard to valuations may be inconsistent with international standards and is likely to lead to reduced valuations and lending for both the property development and agricultural sector. In particular:

- Inconsistency with international and local standards
- Requiring specific valuation methods for agricultural properties.

Each of these is discussed below.

1.1.1 Inconsistency with international and local valuation standards

Restricting valuations to existing use (Attachment A paragraph 16 and Attachment B paragraph 21 & 26) is inconsistent with international standards. This inconsistency is in the current APS 220 Attachment B paragraph 21 (adopt the valuation standard and local standards of the Australian Property Institute) and paragraph 26 (valued on the basis of existing use) and we would request that this conflict be addressed.

Fair Value is defined in International Valuation Standard 2017 (IVS 2017), and International Financial Reporting Standard 13 "Fair Value Measurement" Standards (IFRS 13), and its local equivalent AASB 13) as *"the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date."* (IVS 2017 – General Standards – IVS 104 Bases of Value, paragraph 90.1). This is based on the market value which at IVS 2017 – General Standards – IVS 104 Bases of Value, notes at paragraph 30.4:

> *"The Market Value of an asset will reflect its highest and best use (see paras 140.1 – 140.5). The highest and best use is the use of an asset that maximises its potential and that is possible, legally permissible and financially feasible. The highest and best use may be for continuation of an asset's existing use or for some alternative use. This is determined by the use that a market participant would have in mind for the asset when formulating the price that it would be willing to bid."*

Requiring valuations to be undertaken on only the existing use of a property will significantly reduce valuations for business and the consequent flow of credit. Examples where this could be problematic include subdivision of land, farmers changing their crop or livestock from a lower value product to a higher value product and land redevelopment subject to reasonably likely approval.

Given this, the ABA recommends aligning the final standard with international valuation standards (in consultation with the Australian Property Institute) and removing any requirement for APRA approval for valuations not based on existing use. This would include retaining the fundamental principal that a valuation is the fair value at a point in time. This will mean that the value of a property will vary over the cycle, and that provisioning and capital will be more accurate.

1.1.2 Agricultural valuations

The ABA understands that paragraph 81 regarding the valuation of agricultural land is in response to the Royal Commission Final Report Recommendation 1.12[1]. The final report notes the following:

> *"I consider that APRA should amend APS 220 to provide for valuation of agricultural land in a manner that will recognise, to the extent possible:*
>
> *• the likelihood of external events (including, but not limited to, fire, drought and flood) affecting the land's realisable value; and*
>
> *• the time that may be taken to realise the land by sale at a reasonable price affecting the land's realisable value". (page 102) Vol 1.*

The ABA supports the implementation of the Royal Commission recommendations; however, the recommendation needs to be implemented in a way that is consistent with international valuation standards, recognises operational issues and does not have wider impacts on the agricultural sector. The Royal Commission Final Report provides adequate flexibility for APRA to implement recommendation 1.12 in a way that meets these requirements. The Final Report text intends for APRA to "*recognise, to the extent possible the likelihood of external events"* rather than adopt the exact wording of the recommendation. Given this, the ABA recommends that APRA reconsider the current drafting of paragraph 81 to mitigate the following issues.

[1] Royal Commission into the misconduct in the Banking, Superannuation and Insurance Industry 2018, *Final Report,* Vol. 1 accessed at: https://www.royalcommission.gov.au/sites/default/files/2019-02/fsrc-volume-1-final-report.pdf

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External events

There is concern that the changes recommended by the Hayne Royal Commission may infer that valuers need to go further than current practice – such as predicting likely external events, which is not possible. Further clarity in guidance on this issue would be appreciated to confirm that current practice is compliant with the revised APS 220.

The ABA understands that valuers already take into consideration known environmental issues in their reports. If the property is in a known bushfire, cyclone, flood or subsidence etc. location, then the valuer would note this in the report as a statement of fact, and the related risks would form part of the valuation. The valuer is not able to predict when an 'external event', such as a bushfire, flood, cyclone, storm damage, erosion, mine subsidence, or unknown source of contamination (e.g. gas leak, PFAS, ground water contamination) will occur and unless the market is factoring in such potential events then this will not be reflected in the sales evidence (prices) or the assessed market value.

The definition of external events is wider than environmental events. For example, in the absence of industry guidance, to determine the likelihood of external events, an ADI would need to consider the potential full range of external events. While drought and floods are mentioned, logically commodity market disruptions and/or price fluctuations are also "external events". Further clarification in APS 220 is needed to provide a more specific definition for what events are to be captured by this provision.

Once identified, the impact of external events would need to be operationalised. Guidance would be needed so ADIs can consistently adopt the valuation requirements. This would include guidance on the level of external event risk acceptable to APRA. For example, in the case of floods, should a 1 in 100-year flood or a 1 in 50-year flood scenario be adopted? The type and frequency of events to be considered as part of an ADI's assessment of fair value is likely to significantly impact the adjustment made to agricultural property values at present, and limit further the flow of credit to this sector. Given this, specific guidance will be needed on this proposal.

Specifying different valuation requirements for agricultural property compared to all other assets should be avoided. 'Agricultural land' is not defined and may be open to interpretation. At present, the role of the valuer in assessing market value and identifying and reporting on risk issues is applicable to all mortgage valuations and should not vary across asset types. Applying different valuation philosophies' according by property type is likely to encourage regulatory arbitrage and avoidance, given the lack of an accepted definition.

Given the possible implications from uncertainty about the APS220 valuations wording, the ABA would support APRA working closely with the Australian Property Institute to ensure consistency with international standards and to avoid any unintended consequences on lending. The ABA also considers that further clarification of the intended valuation outcomes from APS 220 in guidance would also reduce uncertainty for all stakeholders.

Alternative policy approaches for external events

The ABA considers an alternate approach to mitigating the concerns of the Royal Commission is for ADIs to consider these possible "external events" in setting the discount factors that are applied internally to fair values and the setting of conservative loan to valuation ratios. The risk appetite could also be used to control geographically based risks, such as limiting lending to high risk postcodes (e.g. maximum LVR thresholds for mining towns).These factors are based on historical experience and judgement and are designed to cover reductions in value that could occur following the origination of the loan from changing conditions over time. These include a forced sale discount, as well as holding and selling costs for the property. Adjustments for the external events contemplated could be accommodated within this framework, rather than distorting the actual market valuation.

1.2 Determining value of collateral

The ABA understands from APRA that upcoming guidance will provide further clarity on the types of documentation that can be used to verify the value of collateral in particular the use of source documents such as Rates Notices and Contracts of Sale.

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1.3 Credit assessment requirements

1.3.1 Regulatory consistency across regulators

The ABA understands that APRA considers that conduct regulatory requirements are consistent across all regulators. In particular that APS 220 conduct related requirements are consistent with ASIC's responsible lending requirements and AFCA's interpretation when assessing a complaint. According to APRA, it takes a macro view of conduct requirements in regulation, whereas ASIC undertakes conduct regulation at the individual or micro level. To ensure regulatory consistency on conduct issues, the ABA supports Royal Commission recommendation 6.9 and 6.10[2] that expects regulators (ASIC and APRA) to coordinate and cooperate. Where possible, regulators should seek to undertake reviews of similar conduct related regulation jointly and use consistent language. The importance of horizontal regulatory cooperation is also reflected in the Australian Government policy implementation principles[3]. This is because cooperation will ensure consistency of interpretation across regulators, full appreciation of impacts on the economy from interventions and provide regulatory certainty for the industry.

One examples where inconsistency between APRA and ASIC wording is that ASIC requires 'reasonable inquiries' in RG 209 (reflecting the wording of the National Consumer Credit Act) whereas APRA in paragraph 38 refers to 'verify the accuracy and completeness of borrower information'.

Regulators also need to consider regulatory consistency with other forms of regulation such as industry codes. The ABA's industry regulation, the Banking Code of Practice, also forms part of the overall regulatory framework concerning credit assessment. Chapter 17 of the Code requires member banks to undertake a responsible approach to lending to individuals and small business (see extract below).

> *49. If we are considering providing you with a new loan, or an increase in a loan limit, we will exercise the care and skill of a diligent and prudent banker.*
>
> *50. If you are an individual customer, that is not a business, we will do this by complying with the law.*
>
> *51. If you are a small business, when assessing whether you can repay the loan we will do so by considering the appropriate circumstances reasonably known to us about:*
>
> - *your financial position; or*
> - *your account conduct.*
>
> *Where reasonable to do so, we may rely on the resources of third parties available to you, provided that the third party has a connection to you (that is, to the small business). For example where the third party is a related entity of yours (including but not limited to your directors, shareholders, trustees, beneficiaries or related body corporates), or is a partner, joint venturer, or guarantor of yours.*

The ABA would also like APRA to consider the consistency of APS 220 conduct risk related requirements to the outcomes of the AFCA's targeted consultation on its approach to responsible lending for business. The ABA understands that AFCA intends to publish a list of banks "lending errors" which would seem to contradict APRA credit assessment requirements as well as proscribe credit risk policies for banks. The ABA would appreciate if APRA could work with AFCA ,ASIC and the ABA to ensure there is a consistent approach to credit assessment across industry.

The ABA looks forward to the publication of the latest ASIC and APRA Memorandum of Understanding to provide further clarity of the split of regulatory responsibilities when it comes to conduct issues and any relevant recommendations from the APRA Capability Review Report.

[2] Royal Commission into the misconduct in the Banking, Superannuation and Insurance Industry 2018, *Final Report,* Vol. 1 accessed at: https://www.royalcommission.gov.au/sites/default/files/2019-02/fsrc-volume-1-final-report.pdf
[3] Australian Government, Prime Minister and Cabinet June 2013, *Cabinet Implementation Unit Toolkit: Governance,* accessed at https://www.pmc.gov.au/sites/default/files/files/pmc/implementation-toolkit-2-governance.pdf

1.3.2 The use of benchmarks (HEM)

The ABA believes that it is good public policy that benchmarks and statistical measures can be used as an element of making reasonable inquiries into and verification of a customer's financial situation. The ABA submits that the use of quality benchmarks and statistical measures can play a role beyond the obligation to take reasonable steps to verify the consumer's financial situation. The industry anticipates that over time, new and more comprehensive benchmarks and statistical measures will be developed based on large data sets that ensure accuracy and better predict risks of financial difficulty and default. It is possible that over time such benchmarks and statistical measures may provide a more accurate way of verifying a consumer's financial situation than relying on self declared customer information and manual verification checks.

The ABA believes that it is against the interest of customers to set policy and regulatory guidance that would unreasonably constrain the ability to use benchmarks and statistical measures to satisfy responsible lending requirements. However, in maintaining flexibility to appropriately use benchmarks and statistical measures, credit providers must take responsibility for the appropriate use, quality and accuracy of such measures. The ABA supports banks taking additional steps to ensure that benchmarks are realistic and to periodically review their use across the portfolio. The ABA believes these kinds of reasonable steps should be applied to future statistical benchmarks and measures.

1.3.3 Proportionate credit assessment

The ABA understands that credit assessments under APS 220 are expected to be proportional to the risk and therefore scalable. The ABA requests that further clarity be provided, whereby the exception of certain products and activities from aspects of the credit assessment is able to be extended at the discretion of the ADI in line with its credit risk management strategy.

1.3.4 Classifying exposures to individuals and non-individuals

The distinction between exposures to individuals and non-individuals is understood, however, it is noted that not all credit assessments will include an assessment of historical financials and future cash flows, and request that the bullet point in paragraph 45 (b) be updated to provide clear guidance, for example by replacing the "and" with "and/or".

1.3.5 References to community expectations

The ABA does not consider that the phrase "community expectations" lends itself to clear legal interpretation, as would be needed in a prudential standard. The ABA understands that APRA expects reputational risk to be considered in credit risk management policies and suggests that reference to community expectations would be better placed in the upcoming APS 220 guidance as it allows APRA to provide more information on how it expects an ADI to interpret this as part of the standard.

2. Asset classification

2.1 Time period for restructured exposures

The time period for restructured exposures is increased from six months to 12 months in APS 220. The ABA understands that APRA made this change to improve consistency with Basel guidance to enable international comparability. While the ABA supports consistency with global standards in most cases, prudential standards need to meet domestic requirements without imposing unnecessary additional cost and burden to borrowers.

The ABA considers that the increase from six to 12 months is unlikely to deliver any additional benefits in terms of minimising risk, but instead will increase costs, as accounts will remain as restructured for a longer period. Data from banks suggests that most restructured exposures return to performing within six months. For example, in one ADI's case, more than 90 per cent of restructured exposures return to performing within six months.

Given this information from banks, the ABA considers there would be little benefit requiring the majority of restructured exposures to remain classified as non-performing for a further six months. Under the draft APS 220, the additional costs in terms of monitoring and capital risk weightings are likely to outweigh the unclear benefits of consistency. The ABA requests that APRA revert back to the original six-month period for restructured exposures in the final prudential standard, due to the proposal being a net cost to the economy.

2.1.1 90 days requirement

The ABA considers that the revised wording concerning the 90 days requirement should be reviewed to reflect that an account is impaired when a facility is 90 days of contracted cash flows overdue. It would be preferred if the wording used in the current APS 220 could be used in the final APS 220 prudential standard as below. This would reduce any potential regulatory uncertainty from the different wording used between the current and revised APS 220. See paragraph 16 of the current APS 220 prudential standard which states:

> *A facility subject to a regular repayment schedule is regarded for the purposes of this Prudential Standard as 90 days past due when:*
>
> *(a) at least 90 calendar days have elapsed since the due date of a contractual payment which has not been met in full; and*
>
> *(b) the total amount unpaid outside contractual arrangements is equivalent to at least 90 days worth of contractual payments.*

At present, the revisions create confusion and uncertainty about whether APRA intends to use the same time period as currently in practice. Using consistent wording supporting the current practice will rectify this issue for banks. Further, clarification of APRA's intended application of the 90 day requirement would be useful in the guidance.

2.1.2 Materiality requirements and exceptions

The ABA considers that the classification of exposures should retain references to 'material' for the ADI's assessment of credit risk. For example, at paragraph 19 in the current APS 220:

> *An ADI must have policies and procedures to ensure timely responses to identified material changes in its credit risk profile.*

ABA understands that APRA intends to include references to material in the final APS 220 prudential standard and the ABA supports this change.

In addition, the ABA questions why APRA has removed the exceptions for certain types of exposures from the reporting of restructured items. The proposed APS 220 does not continue the exemption of agricultural loans from restructured item reporting. Given the seasonal nature of agricultural lending, often loans may be in excess of 90 days behind in contractual payments. Removing the exemption for these kinds of exposures could restrict lending and increase the cost of lending to these groups of customers. This is likely to have significant wider economic impacts given the current softening of the economy.

The ABA recommends that APRA retain the exemption as found in current paragraph 32 (as shown below) in the final APS 220 prudential standard.

> *A non-National Credit Code regulated facility must not be reported as a restructured item where it is placed on restructured terms for less than twelve months due to temporary financial difficulty being experienced by the entity but where long-term viability is unquestioned (e.g. a rural facility encountering a bad season). Such a facility may be treated as non-impaired. The ADI must, however, be reasonably confident that the entity is able to fully perform with no loss of principal and the originally contracted amount of interest or other payments due, and the ADI must not maintain any provisions assessed against the facility on an individual basis.*

2.1.3 Definitions for reporting restructured loans

The ABA recommends that APRA aligns the definitions used for reporting restructured loans with that used in the Basel guidance. The ABA is concerned that the proposed definition is broader than the global (Basel) definition and would therefore lead to a significant and unwarranted increase in the number of customers reported as restructured, potentially leading to higher costs and reduced credit availability for customers. Further, this may affect how international investors and other stakeholders perceive Australian banks.

The proposed restructured definition would also make differentiating between customers that are in real financial distress from those whose facilities are being amended in the normal course of business more difficult. This is likely to lead to operational issues, increases in FTE resources to manage these, and introduces potential ambiguity to current monitoring tools. Taken together, this would be detrimental to an ADI's prudent credit risk management, and negatively impact customers, due to the increase in administration required to manage banking affairs for business customers.

Non-performing credit grades

The ABA would appreciate further guidance on the classifications of *"significantly deteriorated*" and *"non-performing"* restructured exposures. The ABA understands that according to section 3.3 of the Discussion Paper, not all restructured exposures will be allocated "non-performing" credit grades. Instead, some restructured exposures could still be classed as performing. This is because "*Criteria for exit from the restructured exposures category*" refers to exit from the non-performing category. The ABA interprets this paragraph as applying to the reclassification of "non-performing" restructured exposures. The ABA seeks confirmation that paragraph 98 also applies to exit from *"significantly deteriorated"* restructured status.

Definition of financial difficulty

It is currently unclear what the correct definition is to determine financial difficulty and what is meant by restructured in the revised APS 220. Given this, the ABA requests that APRA confirms in guidance whether existing or Basel definitions should be used where applicable. Further, where a definition may not already exist, that APRA provide that definition in guidance.

In addition, the ABA request that APRA provides guidance on the expected treatment and reporting regarding re-ages as restructured debt, including where financial difficulty does not or may no longer apply.

Alternative policy approach

The ABA recommends the following:

- Removing the word "temporary" and providing a definition for financial difficulty (which should be aligned to the definition in the Basel Committee's 2017 Guidelines on Prudential Treatment of Problem Assets, see paragraph 39). This would provide clarity and reduce the scope of reporting, ensuring that Australian banks are not reporting a higher number of restructured facilities than global banks. It would also be helpful to include further guidance in the proposed prudential practice guide.
- Exclude customers whose long-term viability is unquestioned, as per current APS 220 Attachment A, paragraph 32. This would ensure that customers subject to seasonal conditions, such as rural customers, are not automatically reported as impaired (or non-performing under the Draft Prudential Standard) when they cannot meet a principal repayment or repay a seasonal working capital facility. Most of these customers are currently managed on a principal and interest basis, so reporting them as restructured may cause relationship managers to remove the principal payments from contractual arrangements which would be detrimental to prudent risk management.
- Replacing the words "would not otherwise consider" in 12(c)(ii) with "on non-commercial terms" (non-commercial terms being defined as providing a concession to a customer on more favourable terms than what a new customer with a similar risk profile could obtain from the ADI, under current market conditions). This will provide a more objective measure to define a restructure.

- The use of case studies in the proposed prudential practice guide to assist ADIs in interpreting "non-commercial". Examples of cases that could be included are:
    - Lowering the facility interest rate to below the lowest available commercial rate.
    - Extending the facility term for a duration that would result in the facility exceeding the longest available commercial term.
    - Partially charging-off and/or writing-off a portion of the principal.
    - Clarifying when the easing of covenants applies and when this will avert a financial default. Covenants are typically set with minimum headroom to monitor performance and allow an ADI to renegotiate terms and conditions if credit deteriorates.

The ABA notes the existing reporting framework ARF 220 will need to change to align with the new requirements. The ABA would also like clarification as to whether a non-performing customer who is granted concessions under paragraph 12(c) must be reported as restructured as well as non-performing.

2.1.4 Credit evaluation requirement

The ABA considers that guidance is required on an ADI's obligation to complete a credit evaluation as referenced in paragraph 96. This paragraph references the need to have a well-documented credit evaluation, however, it does not note when a credit evaluation must be undertaken. Guidance on when a credit evaluation should be undertaken would clarify this for banks. In particular, guidance should consider the application to new loans not drawn down and how this obligation may be scaled to reflect potential risk.

3. Provisioning

3.1 General reserve for credit losses (GRCL)

The ABA understands that, as per Section 4.3.1 of the discussion paper, the revised APS220 Discussion Paper APS 220, APRA will no longer require ADIs to maintain a general reserve for credit losses (GRCL). This update reflects the introduction of the expected loss approach under AASB 9. The ABA also understands from APRA that a GRCL will continue to be required until the date of implementation of the new APS 220 prudential standard.

The ABA would like APRA to confirm in the final standard consultation paper or guidance that the GRCL will need to be maintained through to the implementation date of the revised APS 220, even notwithstanding that the AASB 9 changes, which facilitate the removal of the GRCL requirement, are already in force.

3.2 Valuation, classification and provisioning

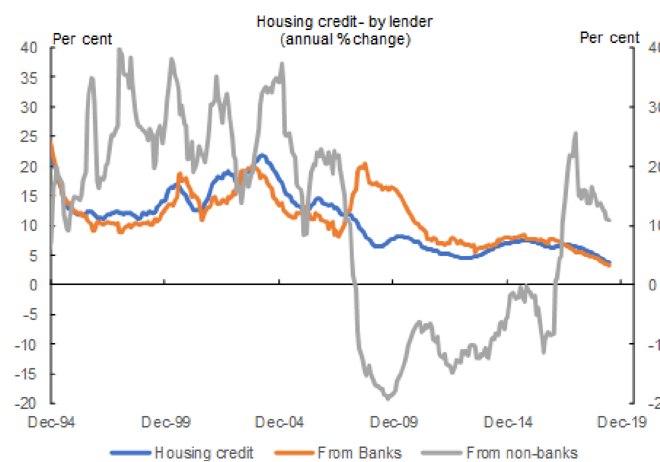
At paragraph 84, APS 220 requires that an ADI must ensure that valuation, classification and provisioning for non-performing exposures are conducted on an individual exposure basis. The ABA requires guidance about 84 how an entity should apply this paragraph 84 to wholesale and retail customers.

At present, banks undertake collective provisioning for retail customers and other small exposures, rather than undertaking provisioning on an individual exposure basis. The ABA understands that APRA expects any valuation, classification and provisioning is undertaken on a proportional basis to risk. Reflecting this intent in guidance could resolve any potential uncertainty from the current drafting of paragraph 84.

4. APRA discretionary limits

APS 220 paragraphs 107 to 108 outline how APRA can use its discretion to implement limits on types of lending, if APRA considers that there is an excessive level or growth in higher risk lending, or credit activity more broadly.

The ABA considers imposing discretionary limits on lending can have severe and important economic consequences. The imposition of limits by APRA between 2014 and 2017 on residential mortgage lending is commonly understood to have contributed to the current softening of the economy and decrease in housing values. The introduction of lending limits in 2017 is associated with sudden strong growth in non-ADI mortgage growth by value, and low growth in ADI mortgages, for the same period (see chart below).



Source: ABA own analysis of RBA data

Given this, the ABA considers that APRA should develop a transparent policy on when and how APRA will impose limits in future. This policy should include how it will:

- Determine when limits are required and provide appropriately rigorous economic analysis supporting this decision.
- Determine the size of the limit and products affected by the limit supported by appropriately rigorous economic analysis.
- Assess the competition impacts of any decision to impose a limit on the relevant product markets affected. In particular, the effects on competition between both ADI and non-ADI suppliers of loans and any consequential impacts on consumers.
- Assess the likely wider economic impacts of the decision in a transparent manner and include relevant consultation with the Council of Financial Regulators.
- Specify a regular review period of any limit. Any review should involve wider industry consultation and the Council of Financial Regulators.

A policy on how APRA will develop and impose limits is consistent with transparent policy practices and will limit any unintended wider economic impacts. The ABA understands that there is a broader internal policy discussion about how APRA uses its enforcement powers and we look forward to providing input to these discussions.

5. Attachment A: Insurance requirements

Attachment A requires insurance of the asset to be maintained under the contractual terms of the exposure. The ABA considers guidance is needed to clarify the level and frequency that ADIs monitor the holding of insurance for the asset. The ABA understands from APRA that it is up to ADIs to determine how frequently insurance is monitored.

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However, the attachment could be interpreted as requiring more frequent monitoring than undertaken at present for some assets. For example, in the case of residential mortgages, the bank confirms in the first year, and makes it a contractual obligation for the term of the loan. It is currently unclear from the draft standard whether current practice would be compliant with the draft standard. If APRA intends further monitoring, this will incur significant additional costs and system changes. Given this, guidance could clarify APRA's intent and potentially avoid significant costs for ADIs.

6. Competition impacts

The ABA considers that APRA should amend is competition assessment for draft APS 220. At present, APRA's assessment suggests that the new APS 220 will not affect competition faced by ADIs in the affected product markets such as residential mortgage lending. However, the new APS 220 increases the regulatory costs/requirements faced by ADIs in comparison to their non-ADI competitors. For example, non-ADIs will not be required to undertake different valuation considerations for agricultural assets, potentially allowing non-ADIs to value properties higher and lend more. This is likely to have negative outcomes for agricultural customers not protected by these requirements. Given this, there is a material decrease in competition in affected product markets where non-ADIs are suppliers. This is because the cost gap between ADIs and non-ADIs will further increase as a result of the new standard, as non-ADIs are not bound by prudential regulation.

While the ABA accepts that prudential regulation of ADIs is appropriate to protect depositors, and non ADIs do not hold deposits, there are several requirements in APS 220 that relate to conduct risk which are present for both ADIs and non-ADIs. Given this, the ABA considers that APRA should review its assessment of competition. Further, the ABA considers that requirements should apply to both ADI and non-ADIs in future. This will ensure that equivalent risks regardless of the activity can be mitigated in the same way which is consistent with international best practice.[4] This will also ensure that regulation does not distort competition negatively for some parts of the market such as ADIs to the benefit of other non-ADI lenders.

Under the current regulatory framework, non-ADIs will have a competitive advantage over ADIs as they would not have a comparable obligation under APS 220. For example, not having to apply the valuation requirements will enable a non-ADI to use a fair market, point in time, valuation, and as a consequence be able to advance more funds against the same property, or offer lower pricing to a customer. Non-ADIs also will not be required to take into account the communities' expectations when dealing with troubled borrowers (paragraph 76).

With the active participation of its member banks in Australia, the Australian Banking Association (ABA) provides analysis, advice and advocacy for the banking industry and contributes to the development of public policy on banking and other financial services. The ABA works with government, regulators and other stakeholders to improve public awareness and understanding of the industry's contribution to the economy and community. It strives to ensure Australia's banking customers continue to benefit from a stable, competitive and accessible banking industry.

Yours faithfully

Karen O'Brien

Policy Director

[4] Bank of International Settlements, 2019, "Chapter III Big tech in finance: opportunities and risks" *Annual Report 2019,* available at https://www.bis.org/publ/arpdf/ar2019e3.pdf

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