



26 April 2017

TO: ALL AUTHORISED DEPOSIT-TAKING INSTITUTIONS (ADIs)

**RESPONSE TO SUBMISSIONS - FINAL REVISED PRUDENTIAL PRACTICE GUIDE APG 120
SECURITISATION**

APRA is releasing the final revised *Prudential Practice Guide APG 120 Securitisation* (APG 120) in response to feedback from industry submissions.

In November 2016, APRA released the final revised *Prudential Standard APS 120 Securitisation* (APS 120) (effective 1 January 2018).¹ APRA also released for consultation a draft revised APG 120.²

APRA received two submissions in response to the draft revised APG 120. APRA's responses to the key matters raised are set out below.

Derivatives transactions

The final revised APS 120 requires ADI swap providers in securitisation schemes to be senior in the cash flow waterfall. The draft revised APG 120 clarifies that this ranking includes where the ADI is a defaulting party under the swap, and for uncollected break costs.

Comments received

Both submissions commented that requiring ADI swap providers to be senior where the ADI is a defaulting party under the swap, and for uncollected break costs, may increase the overall costs of securitisations and reduce the number of swap counterparties that provide swaps to securitisations.

APRA response

APRA has reconsidered this position and has clarified in the final revised APG 120 that swaps may be treated as senior ranking for regulatory capital purposes where the ADI is a defaulting party under the swap, and for uncollected break costs. APRA recognises that default of an ADI swap provider would not necessarily relate to the performance of the underlying exposures. In the case of uncollected break costs, these amounts are at the discretion of the ADI and therefore certainty of cashflow to the securitisation trust, for these amounts, is not assured.

¹ <http://www.apra.gov.au/adi/PrudentialFramework/Pages/Revisions-prudential-framework-securitisation-Nov2016.aspx>

² <http://www.apra.gov.au/adi/PrudentialFramework/Pages/Revisions-APG120-Securitisation-Nov-2016.aspx>

Shared collateral and trust-back agreements

Under the final revised APS 120, trust-back loans (non-securitised loans) are ineligible for risk weights of less than 100 per cent, unless the ADI has a formal second mortgage in regard to the securitised loans used as collateral.

Comments received

Both submissions reiterated that the requirement for an ADI to obtain a formal second mortgage in these circumstances is operationally burdensome and impractical. Both submissions asserted that trust-back agreements are structured to legally operate so as to afford equivalent rights to a formal second mortgage.

APRA response

In light of industry comments, including the operational burden of obtaining formal second mortgages and that shared collateral agreements can be constructed to legally operate so as to afford equivalent rights, APRA has clarified in the final revised APG 120 that, subject to certain conditions, a shared collateral agreement may be considered equivalent to a formal second mortgage for the purposes of APS 120 only.

Warehouse arrangements

The draft revised APG 120 provides some flexibility for originating ADIs to agree a new funding rate to extend a warehouse funding line, provided no other terms and conditions of the securitisation are amended.

Comments received

Both submissions commented that additional flexibility to change the terms and conditions of a warehouse, including credit enhancement and subordination levels and pool parameters, should be permitted for both capital relief and funding-only warehouses.

Both submissions also requested that existing warehouses ineligible for regulatory capital relief should be permitted to be amended prior to 1 January 2018 to minimise increases in regulatory capital requirements under the final revised APS 120. In the absence of this flexibility, the originating ADI may incur substantially higher funding costs.

APRA response

With the exception of self-securitisations, the final revised APS 120 prohibits an ADI from increasing a first loss position or providing a credit enhancement after the inception of a transaction. APRA considers additional flexibility to change the terms and conditions of a warehouse contrary to this requirement.

However, for existing warehouses ineligible for regulatory capital relief, APRA is prepared as a transitional measure to allow ADIs some flexibility to restructure the terms and conditions of these securitisations, provided this occurs by 1 January 2018. APRA supervisors will be in contact with ADIs with respect to any plans to utilise these transitional arrangements.

APRA has released the final revised APG 120 along with this letter. The final revised APG 120 will have effect from 1 January 2018. These documents can be found on APRA's website at:

<http://www.apra.gov.au/adi/PrudentialFramework/Pages/Responses-APG-120-Securitisation-revisions-April-2017.aspx>

Yours sincerely

A handwritten signature in blue ink, appearing to read 'Pat Brennan', with a long horizontal flourish extending to the right.

Pat Brennan
Executive General Manager
Policy and Advice Division