



REGULATORY AGENDA: WHAT'S AHEAD FOR THE AUSTRALIAN MUTUALS SECTOR

AMID MUCH UNCERTAINTY DURING THE COVID-19 PANDEMIC, AUSTRALIA'S REGULATORS FOCUSED ON PROTECTING THE ECONOMY AND SUPPORTING THE FINANCIAL SYSTEM. BOTH ASIC AND APRA SWIFTLY PIVOTED TO MAKE CHANGES TO REGULATORY COMPLIANCE AND SUPERVISION PRIORITIES, DELAYING SEVERAL ACTIVITIES TO ALLOW ENTITIES TO ADDRESS THE IMPACT OF COVID-19.

As we move toward life beyond COVID, regulators have also shifted back into gear, increasing supervision and activity across several key areas for mutual banks in Australia.

STRENGTHENING RESILIENCE AND DRIVING CONTINUITY

APRA continues to strengthen entities' preparedness in managing periods of stress. It includes recovery and resolution planning, operational resilience, stress testing and climate-related financial risks.

A Contingency Planning & Resolution consultation has been scheduled with plans to implement the updated regulation in 2023.

There is a continued and growing focus on cyber security and operational resilience from all regulators. To support this, APRA is developing a new prudential standard focussed on operational risk management accompanied by revisions to CPS 231 Outsourcing, CPS 232 Business Continuity Management and CPS 234 Information Security.

A FOCUS ON GOVERNANCE, CULTURE, REMUNERATION & ACCOUNTABILITY (GCRA)

APRA will continue to prioritise GCRA going forward. There has been significant activity in this space with the update of CPS511 Remuneration released, the pilot Risk Culture Survey concluded and the finalisation of details of the upcoming Financial Accountability Regime. Further to this many consultations regarding key policies have been scheduled for 2022.

LIFTING THE STANDARDS OF PRODUCT GOVERNANCE AND CUSTOMER OUTCOMES

2021 saw the introduction of the new Product Design and Distribution Obligations (DDO). When introducing RG 274, ASIC emphasised the effectiveness of product governance arrangements across the lifecycle of financial products with a focus on supporting better customer outcomes. It ensures a broader range of regulatory activity focusing on the impact of DDO and product governance.

CHANGES IMPACTING CAPITAL RESPONSE

The finalisation of the revised capital framework in response to the Basel III reforms has been a priority for APRA in their quest for ADI capital ratios to be 'unquestionably strong'. Additionally, APRA have expressed concern with problem loans and high-risk portfolios from a credit perspective and have committed to undertaking deep dives in these areas.

Several prudential standard changes in the pipeline will impact the regulatory capital framework. But the most significant for mutual banks is the standardised approach for credit risk - the revised APS 112 *Capital Adequacy – Standardised Approach to Credit Risk* and APS117 *Capital Adequacy - Interest Rate Risk in the Banking Book (IRRBB)*.

A new and higher capital floor applicable to advanced ADIs will positively impact mutual banks as it levels the playing field with advanced ADIs regarding capital requirements.

INTEREST RATE RISK:

APS 117 raises reporting requirements for all ADIs, including the mutuals. We anticipate the following questions and four key challenges to be an important consideration for mutual banks:

1. RESOURCING. Have you formed a clear second line risk function around interest rate risk management? APRA expects risk to have a solid and independent voice concerning IRRBB.

2. BOARD ENGAGEMENT. Does your Board need additional training? Boards will need to play a visible and influential role in the management of interest rate risk.

3. STRESS TESTING AND LIMIT SETTING. Are you adequately prepared to define limits and test scenarios in the current interest rate environment? Comprehensive limits for stress testing, which is likely to challenge the current low-interest environment.

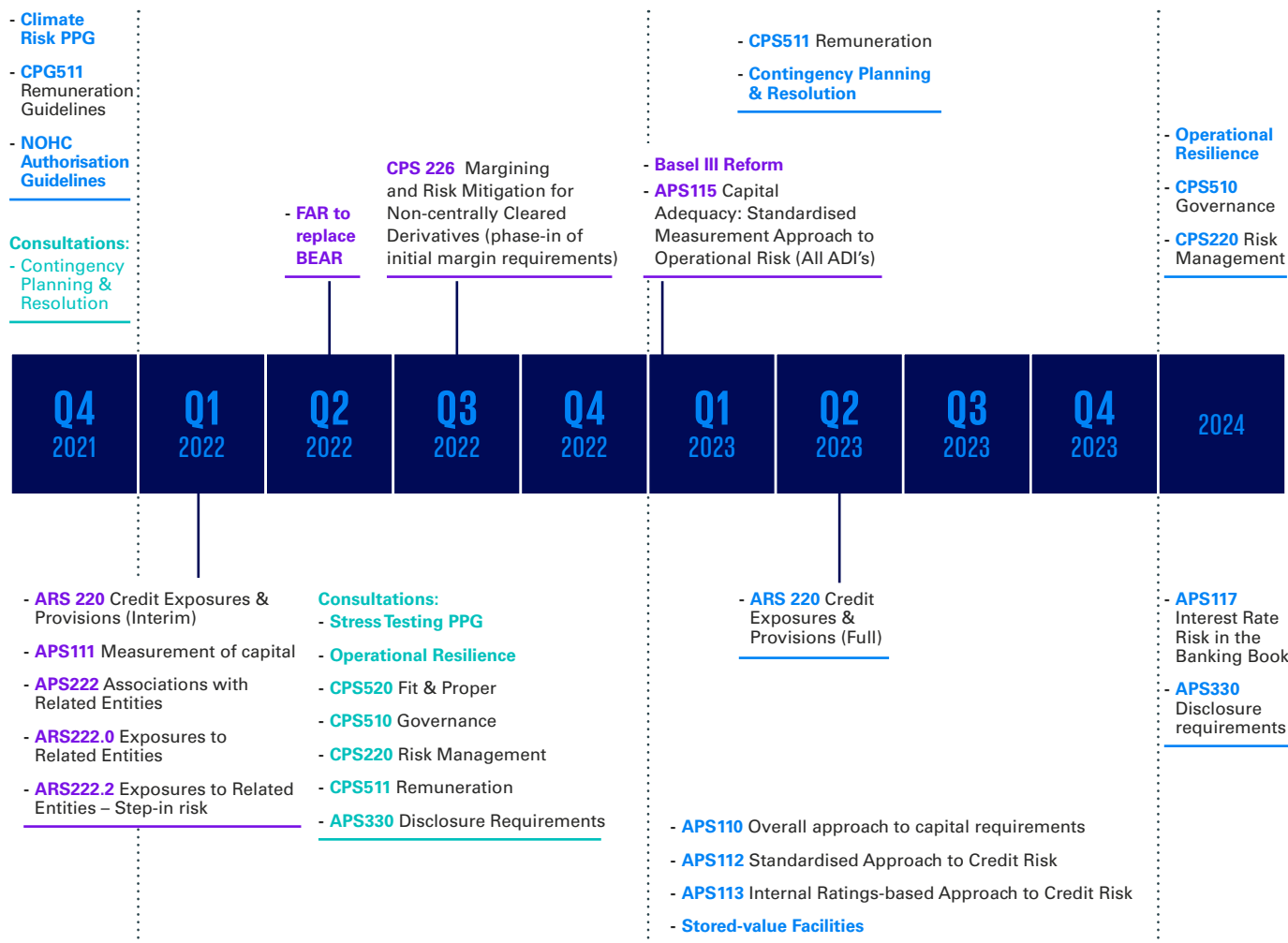
4. DATA AND SYSTEMS. Do you have adequate systems and reliable data? Good decision-making and oversight demand robust systems and reliable data. Many smaller ADIs will need to inject greater rigour into their data and systems.

CALL TO ACTION FOR THE MUTUALS

The next few years will involve intense regulatory changes. The breadth and complexity of these changes will continue to challenge the mutual sector, with the ever-increasing cost of compliance and burden of effort.

While regulators and policymakers focus on financial stability and protecting Australian consumers, they must be mindful of proportionality and ensure they support Australia's competitive and diverse banking market. Accordingly, the mutuals sector must remain agile and respond pragmatically, including through industry collaboration where appropriate.

UPCOMING REGULATIONS



Expected Effective

Confirmed Effective

Consultation Scheduled

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