AFMA

18 April 2017

Manager
Standard Data Collections
Australian Prudential Regulation Authority
GPO Box 9836
SYDNEY NSW 2001

By email: statistics@apra.gov.au

Dear Sir/Madam

Economic and Financial Statistics

The Australian Financial Markets Association (AFMA) welcomes the opportunity to make this further submission commenting on the Economic and Financial Statistics Discussion Paper.

Agencies' Response to Preliminary Submission

AFMA notes APRA's response dated 23 March on behalf of the three agencies to our preliminary submission dated 23 February. AFMA welcomes the extension of the consultation period for phases two and three until 16 May 2017. This submission will nonetheless address issues relevant to phases 1-3.

The agencies' response notes that reporting thresholds are designed to limit the number of forms submitted by the majority of reporting institutions. However, the proposed reporting thresholds have only limited impact on the scope of work required for implementation, even for smaller entities, and AFMA members have indicated that they will need to build systems to monitor compliance with the reporting thresholds and ensure they have the capability to submit data in a timely fashion if these thresholds are reached. Consequently, the compliance burden of the new collection extends well beyond the number of forms actually submitted by reporting entities, so this indicator by itself is inadequate as a guide to the actual change in the reporting burden.

The agencies note the desire of some larger institutions that have enjoyed a longer consultation period to finalise the consultation so that implementation projects can begin. While this is understandable, it is not the position of many AFMA members who have not had the benefit of a longer consultation period, yet face an equally if not more demanding implementation task. It should not be surprising that a staggered, two-tier consultation process gives rise to different levels of preparedness on the part of different reporting entities. The consultation and implementation timetables should make allowance for this.

Whereas larger domestic institutions can prioritise resources locally, many foreign ADIs must compete at a global level for resources to implement the new collection, resulting in additional implementation lags and adjustment costs. Implementation costs typically increase dramatically the shorter the implementation period and the higher the quality of data sought. Operationally, the new collection is more demanding than meeting the LCR requirements that were the subject of a much longer implementation timetable. The EFS implementation timetable adds to the burden imposed by other APRA projects, such as the Liquidity and Large Exposures changes.

We understand the reluctance to adjust the implementation timetable while the consultation remains open. Once the consultation is closed AFMA submit that implementation be delayed until at least 1 July 2019, as argued for in our preliminary submission.

Other Timing Issues

The parallel run as currently proposed is particularly resource intensive, requiring the running of two books that are likely to result in additional queries from APRA, but which may not be reconcilable.

AFMA recommends that the parallel run period should be shortened to three months and conducted on a prospective basis. It is not clear to AFMA members what APRA expects to obtain from the proposed parallel run that cannot be obtained from a shorter run. Greater transparency around what additional data or information will result from the parallel run would also be welcome. There is also concern about the prospect of changes to the collection during the implementation period and dependencies on forms not in scope that may be broken by such changes.

Data Quality, Accuracy and Assurance

Members remain concerned at the exceptionally high level of confidence sought by the new collection that requires costly controls and testing and that exceeds standards required of audited financial statements. The new collection effectively creates two reporting regimes for statistical and prudential purposes, whereas it would preferable to rely on existing reporting frameworks that are already well understood by reporting entities and are internationally comparable. The new collection requires the sourcing and testing of large amounts of non-financial data that does not exist in general ledgers and is a significant contributor to implementation costs.

AFMA submits that APRA consider substituting qualitative reasonable assurance guidance for the quantitative guideline, given there are considerable uncertainties in operationalising the 99% benchmark. The approach taken in Guidance Statement GS 012

Prudential Reporting Requirements for Auditors of Authorised Deposit-taking Institutions from para 81 onwards might serve as a useful model.

In addition to the tightening of assurance framework, members noted ARS702 requests that an audit must be completed within three month of financial year end of the ADI and RFC, including non-disclosing entities. This introduces the inconsistency of an assurance report due date between APS 310 (four months for a non-disclosing entity) and ARS 702 (three months). The different due dates impose an additional resource burden and additional costs on a non-disclosing entity as it must complete the audit one month earlier for the EFS collection. This will also have an impact on the required external auditor resources and the audit schedule. Having regard to these factors, AFMA requests that, for non-disclosing entities, the audit is completed within four month of financial year end, which is consistent with the assurance report due date under APS 310.

Costs of funds

The foreign ADI community queries the usefulness of costs of funds data sought from them by the new collection given that their funding and business profile is fundamentally different to the major domestic institutions, with limited data comparability and constituting a small share of the overall flow of funds.

The lack of comparability arises from the role of matched funding from offshore, the application of bespoke transfer pricing models and specific withholding and corporate taxation rules that apply to this funding. The omission of cost of funds data from the inbound community is unlikely to compromise and could even improve the accuracy of the overall cost of funds data sought. AFMA therefore recommends that the foreign ADI community be carved-out from this element of the collection, for example via reporting thresholds.

Derivatives & Repos

The trade level information sought by the new collection diverges significantly from accounting standards, which is a source of additional costs. AFMA suggests that the derivatives collection be more closely aligned to the trade reporting regime and repo data be moved to a quarterly rather than a monthly frequency. Further cost savings could be achieved by raising the reporting threshold for ARF721 Repo from $100mn to $2bn in line with the business finance/deposit/household financing threshold. To provide perspective on this, the aggregate gross positions of repo dealers in mid-2016 was $205bn.[1]

The $1bn threshold for ARS 722 Derivatives is effectively $500mn at the trade level once the transaction has been hedged, which is less than a single standard trade in some OTC derivatives markets. This threshold should be raised to a significantly higher level that is determined by reference to the scale of the Australian derivatives market[2] and has regard to the national economy purpose of the data. In addition, the technical design of the reporting proposed for exchange traded derivatives warrants further consideration.

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[1] http://www.rba.gov.au/publications/bulletin/2016/sep/5.html
[2] Over $20 trillion in OTC interest derivatives contracts alone were outstanding in April 2017.

Not applying the same confidence standards to the derivatives collection or staggering the application of these standards would also have cost benefits.

There is a strong case to move repo collection from phase 1 to phase 3 alongside derivatives given the substantial work required to implement what is effectively a trade repository. While it is understood this information is sought by the FSB for its global aggregator by the end of 2018, the FSB's requirements should not be prioritised at the expense of domestic objectives and increased project implementation costs. The Council of Financial Regulators (CFR) has recently acknowledged that FSB recommendations concerning securities financing transactions should be applied only in the manner appropriate to the Australian market.[3]

More broadly, it is of concern that a significant new data reporting requirement for derivatives is being contemplated less than two years after the Government's comprehensive trade reporting regime for OTC derivatives came fully into effect. This suggests that it may be beneficial for the CFR and the Government to review the process governing the introduction of new data reporting obligations for financial entities. To achieve its objectives, the national program for financial data and statistics must be conducted in a well-ordered, efficient and cost effective way for all involved.

Cost-Benefit Analysis

Feedback from member firms indicates that the total implementation costs for the industry would be exceptionally high if the proposals in the Discussion Paper were to be implemented in the form currently contemplated. Absent a reconsideration of the proposals, it would in some cases require a significant strategic rebuild of systems to generate and support the data requirements. Initial implementation cost estimates for some smaller institutions and foreign ADIs that have emerged in our industry discussions varied from $5mn to $15mn, depending on the nature of their business and internal information systems. We cannot provide an industry level implementation cost estimate at this stage, in part as some banks are still making their internal assessment, but we expect that a number will provide estimates for their firm in their own submission.

Feedback from member firms also indicates that the dollar cost of implementation costs is naturally lower for small banks (eg foreign ADIs) than for the largest banks but the *relative* cost for them is far higher. A more practical approach to data quality, reporting thresholds and implementation timeframes would materially reduce implementation costs and help to address these issues.

The proposed new collection constitutes a significant piece of economic infrastructure and it is important that the economic value of the new collection is maximised to offset the additional costs of collection.

In addition to the measures recommended above to reduce costs, it is important that steps are taken by the three agencies to ensure that the new collection yields clearly identifiable additional benefits for regulators and industry.

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[3] http://www.rba.gov.au/publications/fsr/2017/apr/pdf/dev-fin-sys-arch.pdf

As things stand, there is inadequate transparency around the benefits APRA, the ABS and RBA expect to obtain from the new collection. While it is superficially appealing to argue that improving the scope and quality of data collected will improve public and private decision-making, how this will be achieved is not canvassed in detail in the Discussion Paper. In particular, it would be useful to understand what additional data will be published as a result of the new collection and how it is anticipated that this will benefit both the public and private sectors.

For example, it would be desirable if the new collection led to the publication of monetary aggregates, since these are widely acknowledged to be more informative than unweighted aggregates, especially for monetary policy purposes. While it is possible to calculate such aggregates based on existing published data, an official series of weighted aggregates based on the new collection would be a welcome addition to the data currently published by the RBA.

Experience with trade reporting and central clearing mandates, which were adopted at considerable expense to industry, has been that the volume of data submitted to regulators has not seen a commensurate increase in the release of additional data by regulators that would assist, for example, in measuring market quality or the quality of trade execution.

In its submission to the Productivity Commission's inquiry into Data Availability and Use, AFMA recommended that the CFR develop a comprehensive data dissemination framework to ensure that the economic value of the growing quantity of data held by regulators and collected at a cost to industry and the community is maximised. It would be helpful to AFMA members to better understand how the new collection would achieve this.

Industry Working Groups

AFMA supports the project objectives and is keen to assist in delivery of the outcomes in an efficient and timely way, as discussed during the consultation meeting with the agencies on 13 April 2017. We believe industry participants can contribute constructively to the design and content of the project implementation plan. The agencies would benefit from being able to draw on industry's practical market knowledge (business and operational) and also the project management and implementation experience of its participants in setting time frames and calibrating critical inputs like reporting thresholds.

We have noted above the generally high level and quite limited explanation of the objectives of the proposals and the manner in which the proposed measures will resolve the perceived problems. With the benefit of a deeper insight from agencies into these matters, industry participants would be better placed to contribute to the design of more effective, efficient and timely solutions.

With this in mind, we recommend close ongoing engagement by the agencies with industry practitioners including through working groups on specific matters including derivatives, repo and securities lending and cost of funds reports. AFMA believes that this process should commence without delay to build good momentum in delivery of the project's objectives.

Project Governance

The project to modernise the economic and financial statistics involves a substantial resource commitment by banking and finance industry in the expectation of it delivering significant public benefits through the agencies, largely in the form of better economic policy analysis. The weak connectivity between the direct incidence of project costs and the beneficiaries, including the agencies, creates a moral hazard risk that the governance process must manage.

In addition, there are significant practical challenges to be overcome for the successful design and implementation of the project, which will require sound judgment and the careful balancing of strategic objectives. A solid project information base will support this decision making process and this can be enhanced by a having effective ongoing communications between the agencies and industry to facilitate the exchange of the relevant information.

Having regard to these factors and the complexity of inter-agency engagement, it is appropriate that the CFR is the sponsor of the project. The scale and relevance of the project, and the risks in its implementation, means that it must be given active oversight at the highest level within the Council.

Therefore, we request that an appropriate high level governance process for the project within the Council should be established or confirmed and that there should be regular, periodic liaison with an appropriate group of senior industry representatives at this level during the project design and implementation period.

Conclusion

AFMA members are happy to provide further feedback on any of the above issues.

Yours sincerely

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