

## 4. Domestic Regulatory Developments

Australia's key financial regulatory agencies – the Australian Prudential Regulation Authority (APRA), the Australian Securities and Investments Commission (ASIC), the Australian Treasury and the Reserve Bank of Australia – coordinate their activities via the Council of Financial Regulators (CFR). The CFR is chaired by the Bank, which also provides the secretariat. CFR agency heads meet quarterly; ongoing inter-agency collaboration occurs through a number of working groups, complementing the frequent informal bilateral contact between individual agencies.

In light of the resurgence of COVID-19 cases and renewed lockdowns in a number of states and territories, the CFR is once again closely monitoring the impact of the pandemic on the resilience of households, businesses and the financial system. While CFR members expect the economy will bounce back as vaccination rates increase and restrictions are eased, they remain alert to pockets of stress that may cause hardship and restrain the eventual recovery. The CFR welcomes the role that financial institutions are once more playing in supporting affected households and businesses, including by offering temporary loan payment deferrals. The CFR is closely monitoring risks relating to trends in household debt. Further, it has been discussing the financial risks from climate change and regulatory arrangements for electronic conveyancing and stablecoins. The CFR has engaged other Australian regulators in some of these important discussions.

### The effects of the pandemic have once again been a key focus of the CFR ...

The recent lockdowns across several states and territories have led to a renewed focus by the CFR agencies on the effects of the pandemic on households, businesses and the financial sector. The CFR discussed these developments at its September 2021 meeting. As outlined in the earlier chapters of this *Financial Stability Review*, all three of these sectors entered this new period of lockdowns in a sound financial position, reflecting earlier support measures and the strength of the economic recovery to that point. This allowed lenders to again extend support to borrowers through loan payment deferrals, though in a more targeted way. Loan payment deferrals were again supported by regulatory relief provided by APRA. These measures have been working in conjunction with financial relief provided by the federal and state governments.

While there are isolated pockets of stress among households and businesses – some of which may persist for some time – CFR members remain confident that the economy will recover well once restrictions are eased. The financial sector is expected to remain healthy and well positioned to support a robust expansion from late 2021.

CFR members also discussed progress in settling the legal validity of business interruption insurance (BI) claims for businesses affected by the pandemic. An initial test case was finalised in June 2021 – it found that insurers could not rely on policy exclusions referencing the repealed

*Quarantine Act 1908*. Another test case is underway to clarify the interpretation of other details in Bill policies. The CFR has encouraged insurers to proactively reach out to policy holders and settle valid claims quickly and efficiently once legal clarity has been established.

### **... as well as monitoring household borrowing and the housing market**

The CFR closely monitors credit conditions, with housing credit a focus in 2021. As discussed in 'Chapter 2: Household and Business Finances in Australia', housing borrowing continued to pick up over the first half of the year, with strong housing market activity in most markets. In the context of very low interest rates and rising housing prices, CFR members have stressed the importance of maintaining sound lending standards. More broadly, members are carefully monitoring trends in household debt, and have discussed policy options to target growing risks due to household borrowing outpacing incomes. In early October, APRA announced that it would increase the serviceability assessment rate it expects banks to use when assessing prospective borrowers' home loan applications (see 'Chapter 5: Mortgage Macroprudential Policies'). This action, which will increase the resilience of borrowers, was supported by the other CFR members. Given the increased focus on macroprudential measures in Australia and overseas, APRA will also soon release a paper on its framework for macroprudential policy.

### **CFR agencies are working with the industry to understand and assess climate change-related financial risks**

The risks to the financial system from climate change are a growing focus of the CFR. Financial institutions, particularly banks and insurers, are exposed to physical, transition and legal climate risks that need to be proactively managed. In addition, climate change and institutions'

responses are increasingly influencing the capital allocation decisions of many investors; this could have implications across the financial system and the real economy. These developments highlight the need for regulators and financial institutions to understand and manage climate change risks, which in turn requires robust disclosure of those risks.

The CFR agencies' activities to promote understanding, transparency and management of climate change-related risks are coordinated through the CFR Working Group on Financial Implications of Climate Change. A substantial program of work is currently under way (see 'Box A: Australian Financial Regulators' Actions on Climate Change-related Risks'). The CFR strongly supports and regularly discusses this work, as well as the ongoing constructive engagement between regulators and financial institutions on this topic.

### **Financial regulation is adapting to innovation and evolving needs**

With financial technologies and business models continuing to evolve, a priority for both the government and CFR members has been to ensure that regulatory frameworks continue to encourage innovation, while maintaining their effectiveness and a level playing field. The CFR agencies have therefore sought to cooperate on the development of regulatory approaches to a range of innovations – in some cases, in conjunction with agencies outside the CFR.

A range of recent innovations have related to the payments system. For this reason, the CFR has discussed on several occasions the government's Payments System Review and the Reserve Bank's Review of Retail Payments Regulation. Both reviews recognise the need for the regulatory framework to respond to the evolving nature of the payments landscape. The final report of the Payments System Review, in particular, noted that regulatory and governance arrangements could be enhanced to reduce

complexity and be positioned to adapt to new challenges and opportunities. Key recommendations included:

- a greater role for the Australian Government in setting the strategic direction of the payments ecosystem, in collaboration with regulators and industry
- increasing flexibility to regulate new and emerging payment systems, including by expanding the Bank's ability to designate payment systems and by introducing a new designation power for the Treasurer, guided by national interest concerns
- introducing a tiered licensing framework, which would apply to defined regulated activities and make it easier for payment providers to seek authorisation and access payment systems.

The CFR discussed the recommendations at its September meeting, including their relevance to other CFR work streams. Members are also contributing to Treasury's consultation on the recommendations.

The Bank's Review of Retail Payments Regulation has been focused on the regulatory framework for card payments, along with broader issues arising from new entrants and innovation in retail payments. The Bank issued a consultation paper presenting preliminary conclusions in May 2021, which covered: issuance of dual-network debit cards and promotion of 'least-cost routing' of debit card transactions; debit card interchange fees; transparency of card network 'scheme fees'; and surcharging of 'buy now, pay later' systems. The final conclusions of the review will be released in coming weeks.

Earlier in 2021, the CFR formed a working group to investigate the regulatory implications of stablecoins – a type of crypto-asset that aims to maintain a stable value against one or more currencies or assets. While there has been almost no issuance of Australian dollar-denominated stablecoins and their use as a

payment method in Australia has been very limited, new arrangements could emerge that gain rapid adoption. The CFR has discussed the consumer and financial system risks related to stablecoins, as well as international regulatory developments. In light of increased activity in crypto-assets more broadly, the working group will merge with an existing group focused on distributed ledger technology, and examine possible regulatory arrangements in Australia for crypto-assets, including stablecoins. This will take into account the findings of the Payments System Review, earlier CFR recommendations on the regulation of stored-value facilities, and other recent developments.

CFR agencies have been working with other Australian regulators to address challenges in cross-border payments. This work has included coordinating on Australia's contribution to the Roadmap for Enhancing Cross-border Payments that has been developed by the Financial Stability Board (FSB) for the G20. The Roadmap is a five-year program of goals, milestones and responsibilities to address various frictions in wholesale and retail cross-border payment arrangements. These frictions contribute to the key challenges that end users and service providers of cross-border payments face – namely, high cost, low speed, limited access and insufficient transparency. The Bank is contributing to a number of Roadmap working groups, including those focused on: improving access to payment systems for new cross-border payment service providers; standardising payment messaging practices; and exploring issues presented by possible new infrastructure for cross-border payments, such as global stablecoins and central bank digital currencies. The G20 has requested that the FSB monitor progress and report annually, with the first progress report due in coming weeks.

A related issue has been the withdrawal of banking services ('de-banking') from some non-bank payments and other financial service

providers. This has included some remittance providers and financial technology companies. At a meeting with other government agencies in June 2021 (see below), the CFR discussed trends in, and the drivers of, de-banking, including the role of ‘know-your-customer’ obligations. A working group has been established to consider these issues in more depth and to investigate the feasibility of policy responses.

### Regulation of financial market infrastructures will be enhanced

In June this year, the Australian Government announced that it would introduce reforms to the regulation of financial market infrastructures. The CFR welcomed this decision. The Bank worked with other regulators through the CFR to develop proposals for reforms to the regulation of clearing and settlement (CS) facilities, markets, trade repositories and benchmark administrators. The CFR consulted on these in 2019, before providing advice to the government in 2020.<sup>[1]</sup> The reforms aim to support the effective regulation of the systems, services and facilities that underpin Australia’s financial system by strengthening the supervision and enforcement powers of ASIC and the Bank. CFR members will continue to engage closely as legislative reforms are developed.

Importantly, the reforms introduce a crisis management regime for licensed CS facilities. As part of this, the Bank would have a key role as the resolution authority for CS facilities; it would have the power to intervene in a distressed domestic CS facility in order to ensure that the facility’s critical functions continue to operate.

The regime will include powers and obligations to allow the Bank to prepare resolution plans and require providers of critical CS services to operate in a way that is consistent with effective resolution. Key resolution powers will include: giving a direction to a CS facility to take a

specified action; appointing a statutory manager; and transferring a facility to new ownership. If necessary for resolution to be effective, these powers may also be used over companies related to the CS facility licensee. The resolution regime will include a \$5 billion standing appropriation that may be used as a last resort, with Ministerial approval, to provide temporary funding to support resolution.

### Work on cyber-security and other focus areas is progressing

Cyber-security in the financial sector is also a major focus of the CFR. The CFR’s Cyber Security Working Group is developing a Cyber Attack Incident Response Protocol, which will coordinate CFR agencies’ responses to a significant cyber-attack affecting one or many regulated entities. Agencies continue to refine and test a draft Protocol, which is expected to be finalised in coming months. CFR agencies are also working closely with the Department of Home Affairs on the development of new cyber-security obligations for ‘critical infrastructure’ assets; legislation that would enable the reforms is currently before Parliament. The reforms will bring financial services and markets within the scope of Australia’s critical infrastructure regime, and could place additional cyber-security obligations on the most critical entities in the financial sector. CFR agencies are working to ensure the new regime is as aligned as possible with existing cyber-security obligations placed on financial sector entities, including APRA standards. The Bank is also assisting the Department of Home Affairs to apply the reforms to the central operators of critical retail payment systems.

In June 2021, the CFR considered the recommendations of a working group formed to review the regulatory framework for financial settlement aspects of property e-conveyancing. The working group was comprised of CFR agencies, the Australian Competition and

Consumer Commission (ACCC) and state land title registrars. While there are well-developed governance and regulatory arrangements for the land titling aspects of e-conveyancing, the working group identified some areas where the regulation of financial payment and settlement aspects could be enhanced to promote consumer protection, resilience and competition in the e-conveyancing market. The CFR endorsed the working group's key recommendation that the e-conveyancing industry adopt a self-regulatory regime (comparable to arrangements for some payment clearing streams), governed by an industry code. Separate to the CFR's work on financial settlement in e-conveyancing, state land title registrars are currently developing a framework for interoperability between e-conveyancing platform providers, including new entrants. The CFR expects the industry code to be in place by September 2022, following the implementation of interoperability reforms.

### The CFR engages with other regulators in Australia and New Zealand

The roles and interests of CFR agencies often intersect with other regulators, so the CFR

engages more broadly whenever appropriate. An important means of extending its coordination arrangements is via an annual meeting with other Australian regulators with an interest in the financial sector, notably the ACCC, the Australian Taxation Office and the Australian Transaction Reports and Analysis Centre. The most recent meeting occurred in June 2021. Topics discussed included agencies' actions to support recovery from the pandemic, cross-border payments, de-banking and regulation of stablecoins. Representatives of the ACCC also separately attend CFR meetings where appropriate, including recently for discussions of housing market risks and responses, as well as e-conveyancing.

The CFR agencies meet with their New Zealand counterparts through the Trans-Tasman Council on Banking Supervision (TTBC). The TTBC currently meets separately at the agency heads, deputies and working levels. The TTBC Heads met most recently in June 2021 and discussed economic conditions, cyber resilience, climate change risks to the financial system and bank resolution arrangements.

### Endnotes

[1] For the CFR's Advice to Government and its Response to Consultation, which addressed submissions on the 2019 consultation paper on the proposed reforms, see CFR (2021), 'Financial Market Infrastructure

Regulatory Reforms: Response to Consultation and Advice to Government', Media Release No 2021-02, 8 June. Available at <<https://www.cfr.gov.au/news/2021/mr-21-02.html>>.