

## Article Information

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## APRA consulting with ADIs on APP 223

### APRA has written to all ADIs regarding a consultation on revisions to APP 223 Residential Mortgage Lending

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On 21 May 2019, APRA wrote to all Authorised Deposit-Taking Institutions regarding consultation on revisions to Prudential Practice Guide APP 223 Residential Mortgage Lending (**APP 223**).[\[1\]](#)

Since 2014, APRA has specified that a prudent ADI's serviceability assessments should incorporate a buffer of at least 2% above the loan product rate and a minimum floor rate of at least 7%, with prudent practice to maintain a buffer and floor rate above these levels.[\[2\]](#) The purpose of this guidance is to ensure borrowers are able to continue to service and repay their loans if interest rates were to rise,[\[3\]](#) as well as adding a degree of conservatism to the serviceability assessment process.

APRA believes that the measures introduced in 2014 have serviced an important purpose in the environment of low interest rates and high household debt.[\[4\]](#) However, due to the changing nature of the market, APRA considers it appropriate to review the current guidance, particularly due to:

1. the low interest rate environment likely to extend further than originally anticipated, meaning the gap between actual rates paid and the floor rate to be unnecessarily wide; and
2. ADIs have now introduced differential pricing for mortgage products.[\[5\]](#)

In response, APRA proposes to:

3. remove the quantitative guidance on the level of the serviceability floor rate, i.e. the reference to a specific 7 per cent floor. APRA will still expect ADIs to determine, and keep under regular review, their own level of floor rate, but ADIs will be able to choose a prudent level based on their own portfolio mix, risk appetite and other circumstances;
4. increase the expected level of the serviceability buffer from at least 2 per cent (most ADIs currently use 2.25 per cent) to 2.5 per cent, to maintain prudence in overall serviceability assessments; and
5. remove the expectation that a prudent ADI would use a buffer 'comfortably above' the proposed 2.5 per cent, to improve clarity of the prudential guidance;

in an effort to provide greater flexibility to ADIs to manage and set floor rates that reflect the outlook of interest rates, whilst still ensuring prudence is maintained for serviceability.[\[6\]](#)

Alternatively, APRA considered retaining but reducing the interest rate floor, and leaving the current interest rate buffer unchanged. However, APRA believed this would not properly address the emergence of differential pricing.[\[7\]](#)

Feedback on the draft revisions are open for a four-week public consultation, until 18 June 2019.

#### CONCLUSION / CALL TO ACTION

*Try to conclude the article by outlining the key points or action items that the reader should take away with them.*

[\[1\]](#) APRA, 'Consultation on revisions to Prudential Practice Guide APG 223 Residential Mortgage Lending' (Letter, 21 May 2019),

[https://www.apra.gov.au/sites/default/files/letter\\_consultation\\_on\\_revisions\\_to\\_prudential\\_practice\\_guide\\_apg\\_223\\_residential\\_mortgage\\_lending.pdf](https://www.apra.gov.au/sites/default/files/letter_consultation_on_revisions_to_prudential_practice_guide_apg_223_residential_mortgage_lending.pdf).

[2] APRA, 'Reinforcing sound residential mortgage lending practices' (Letter, 9 December 2014), <https://www.apra.gov.au/sites/default/files/141209-Letter-to-ADIs-reinforcing-sound-residential-mortgage-lendingpractices.pdf>.

[3] APRA, Prudential Practice Guide APG 223 Residential Mortgage Lending (February 2017) [https://www.apra.gov.au/sites/default/files/APG-223\\_0.pdf](https://www.apra.gov.au/sites/default/files/APG-223_0.pdf).

[4] APRA, 'Consultation on revisions to Prudential Practice Guide APG 223 Residential Mortgage Lending' (Letter, 21 May 2019), [https://www.apra.gov.au/sites/default/files/letter\\_consultation\\_on\\_revisions\\_to\\_prudential\\_practice\\_guide\\_apg\\_223\\_residential\\_mortgage\\_lending.pdf](https://www.apra.gov.au/sites/default/files/letter_consultation_on_revisions_to_prudential_practice_guide_apg_223_residential_mortgage_lending.pdf).

[5] Ibid.

[6] Ibid.

[7] Ibid.