General Insurance Reform Bill 2001
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General Insurance Reform Bill 2001

Date Introduced: 28 July 2001
House: House of Representatives
Portfolio: Treasury

Commencement: The substantive amendments proposed by the Bill to the Insurance Act 1973 are taken to have commenced on 1 July 2002. The transitional provisions contained in Schedule 2 of the Bill commence on Royal Assent.

Purpose

The major amendments proposed by the Bill:

• provide the Australian Prudential Regulation Authority (APRA) with power to make, vary and revoke prudential standards

• expand the coverage of the Insurance Act 1973 to include the non-operating holding companies (NOHC) of a general insurer, and the subsidiaries of a general insurer and NOHC

• expand the obligations on auditors and actuaries to report to APRA, in particular to require auditors and actuaries to inform APRA where he/she has reasonable grounds for believing certain matters have occurred including that the insurer, NOHC or a subsidiary is insolvent, or there is a significant risk that it will become insolvent

• require general insurers to appoint APRA approved auditors and actuaries, and

• provide APRA with power to remove certain directors and senior managers of insurers and their subsidiaries where satisfied the person is a disqualified person, or does not meet one or more of the criteria for fitness and propriety set out in the prudential standards.
Background

What is insurance

The principal function of insurance can be said to be to

provide financial protection against the consequences of events, the occurrence of which is generally adverse to the interests of the person effecting the insurance (the insured), although events which mature life insurance policies are not always adverse. This is achieved by risk transference and distribution. By effecting insurance, insureds transfer the risk of economic loss to insurers, who in turn redistribute the risk through investment and reinsurance arrangements. Thus the adverse effect of economic losses is minimised by distributing the risk.¹

The Federal Court of Australia considered what constitutes insurance in Australian Health Insurance Association Limited v Esso Australia Limited.² In its majority judgement the Court held that the word insurance must be taken by its defined meaning and:

• The essence of the relationship between insurer and insured is the relationship of indemnity in the context of contingent loss. If a contract has the hallmarks of an insurance contract, the contract will be one of insurance

• Proportionality of the premium to the risk undertaken may help to distinguish the concept of insurance from other concepts but it is not an indispensable element. All that is necessary is the undertaking by the insurer for good consideration, and

• The absence of profit from an activity does not disqualify that activity as a business; nor the fact that the activity is carried on as part of a much broader activity.³

Insurance is classified in a number of ways. Most commonly insurance is classified by way of the event insured against, for example, into categories of life, fire, marine and accident. A broader classification, and one which is reflected in legislative regimes, is to distinguish indemnity insurance from contingency insurance. Under indemnity insurance, the insurer agrees to indemnify the insured on the latter having a loss. All contracts of insurance are indemnity contracts, except for contracts of life, sickness and personal accident insurance. The latter come within the contingency classification whereby an agreed sum is paid when the event insured against, for example death, occurs. This division between non-life (general insurance) and life insurance is the main distinction or category division in relation to the regulation of the Australian insurance industry.

The Constitution provides the Australian Parliament with the power to pass laws with respect to certain specified areas. Insurance is specifically dealt by section 51(xiv) of the Constitution, which provides that:

The Parliament shall, subject to the Constitution, have power to make laws for the peace, order and good government of the Commonwealth with respect to

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Insurance, other than State insurance; also State insurance extending beyond the limits of the State concerned.

While the Commonwealth’s *Life Insurance Act 1995* is applicable to State insurance which goes beyond the limits of the relevant State concerned, the *Insurance Act 1973* does not. The Australian Parliament has not elected to date to exercise its power over State insurance extending beyond the limits of the relevant State concerned. While there is only limited High Court opinion on the meaning of section 51(xiv), it is clear that section 51(xiv) empowers the Australian Parliament to legislate in respect to all aspects of insurance (including the conditions upon which any person or corporation may carry on insurance business of any kind and to establish mechanisms for the day to day supervision of such persons and corporations and to regulate their financial affairs), other than State insurance.

**Australian statutory regulation**

The conduct of the Australian insurance industry is regulated by both Federal and State legislation. The applicable laws apply to insurers only if they carry on insurance business. While life insurance is regulated by the *Life Insurance Act 1995*, most non-life or general insurance is regulated by the *Insurance Act 1973*.

The responsibility for overseeing the regulatory system and monitoring the activities of insurance companies which issue general and life insurance policies is statutorily vested with APRA.

An insurer may carry on general insurance business in Australia only if authorised to do so under the *Insurance Act 1973*. Section 3(1) of the *Insurance Act 1973* defines an insurance business to mean:

> the business of undertaking liability, by way of insurance (including reinsurance), in respect of any loss or damage, including liability to pay damages or compensation contingent upon the happening of a specified event, and includes any business incidental to insurance business as so defined,

The *Insurance Act 1973* does not apply to certain forms of insurance business, including:

- life insurance business
- accident insurance business undertaken solely in connection with life insurance business
- pecuniary loss business carried on solely in the course of banking business
- benefits provided by friendly societies, trade unions and employee associations for their members and their members’ dependants
employer and employee provided superannuation, pension, retirement, disability and death benefits

funeral benefits

business undertaken by carrier, carriers’ agents, forwarding agents, warehouseman and shipping agents in respect to other people’s goods which are within their control for the purposes of carriage, storage or sale

business undertaken by innkeepers and lodging-house keepers in respect of goods deposited with them for safe custody or which a guest hold for another person

insurance of the property of a religious organisation, and

health insurance provided by a registered organisation.6

APRA may grant an authority to carry on general insurance business under the Insurance Act 1973 if:

• an applicant’s paid up share capital is at least $2 million

• where the applicant is incorporated in Australia, its assets exceed its liabilities by at least $2 million

• the applicant’s assets in Australia exceed its liabilities by at least $2 million

• the applicant’s arrangement for reinsurance have been approved by APRA or it has been granted an exemption

• the applicant can and is likely to be able to continue to meet its liabilities, and

• the applicant complies and is likely to be able to continue to comply with the provisions of the Insurance Act 1973.7

Under section 51 of the Insurance Act 1973, APRA is accorded power to investigate and supervise the affairs of an authorised insurer where it appears that the insurer cannot or may not be able to meet its liabilities.

APRA or an appointed inspector is accorded extensive powers under the Insurance Act 1973 to investigate an authorised insurer. For example, APRA or an inspector may:

• investigate another corporation that is or has been associated with the insurer

• enter land or premises occupied by the insurer being investigated to examine and take possession of papers relating to its affairs

• compel a prescribed person to produce papers relating to the affairs of the insurer being investigated, and which are in under the person’s custody or control, and to

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appear before APRA or the inspector for examination concerning the matter being investigated, and

- compel a prescribed person to give all reasonable assistance concerning the matter being investigated.\textsuperscript{8}

APRA may revoke an insurer’s authority to carry on general insurance either at the insurer’s request where APRA is satisfied that the insurer has no liabilities in respect of insurance business in Australia, or the insurer has transferred all interests in its insurance business in Australia to another authorised insurer.\textsuperscript{9} Additionally, APRA with the Treasurer’s approval, may revoke an insurer’s authority if the insurer does not start business to carry on insurance business in Australia within 12 months of being authorised to do so, or has not carried on insurance business in Australia during the last 12 months and has no liabilities in respect of such business.\textsuperscript{10}

The \textit{Insurance Act 1973} imposes a number of conditions on authorised insurers, including

- a requirement to maintain solvency margins

- if an insurer has a share capital, maintain its paid up share capital at no less than $2 million

- comply with any conditions that APRA or the Treasurer imposes on its authority, and

- where the corporation is incorporated in Australia, a condition that:
  - the value of its assets at all times exceed the amount of its liabilities by not less than $2 million, or
  - 20\% of its premium income during its last preceding financial year, or
  - 15\% of its outstanding claims provision as at the end of its last preceding financial year

whichever is the greatest.\textsuperscript{11}

\textbf{Key industry data}

\textbf{For the December Quarter 2000:}

- Total private sector general insurers assets increased to $63.1 billion by the end of December 2000, representing an increase of 1.7\% during the quarter, or 7.7\% over the previous year.

- Private sector general insurers premium revenue (less reinsurance expense) was $3.8 billion for the December 2000 quarter, up 4.1\% on the September 2000 quarter. Premium revenue for the year to December 2000 amounted to $14.6 billion, up 1.8\% (or $258 million) on the previous year.
– Private sector general insurers claims expense (less reinsurance and other recoveries revenue) were $2.8 billion for the December 2000 quarter, down 10.6% on the September 2000 quarter. Claims expense for the year to December 2000 amounted to $12.2 billion, down 8.3% (or $1.1 billion) on the previous year.

– Net premium flows (that is, premium revenue less claims expense) for the year to December 2000 were $2.4 billion, up 127.8% (or $1.4 billion) on the previous 12 months.

– The underwriting result (that is, premium revenue less claims and underwriting expenses) for the year to December 2000 was minimum $1.6 billion, a 42.3% (or $1.2 billion) improvement on the previous 12 months.12

Industry reaction

The peak insurance industry body, the Insurance Council of Australia (ICA), established a major working party in 1999 as part of the Federal Government’s review of the Insurance Act 1973.13 The ICA maintains that it has consistently supported changes to the prudential regulatory regime through a review of the Insurance Act 1973 which has been conducted over the last two/three years.14 In May 2001 the ICA responded to Treasury’s Discussion Paper regarding the Insurance Act Amendment Bill 2001. Key recommendations in the ICA’s response included:

Recommendation – Division 3 – Revocation of Authority

In relation to breaches of legislation including failure to pay levies and the like, although it is recognised that an ultimate sanction of revocation of authority will be required, we would have thought that this is better dealt with through other explicit penalty provisions.

We strongly support the introduction into legislation of provisions which would allow the transfer of portfolios of business both in anticipation of the handing in of an authority or for other business purposes. This would greatly simplify the disposition and acquisition of insurance businesses in Australia.

Care needs to be taken in drafting any provision requiring notification to policyholders to properly allow for issues relating to the identification of those persons and the location of them.

We generally believe that any power to grant relief from the application of any part of the Act should also be exercised having regard to competition policies so that a particular company should not, by operation of this provision, be able to obtain a competitive advantage.

Recommendation – Section 7 APRA may determine that provision of the Act do not apply

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The power to grant relief from the operation of the provisions of the Act should not be permitted to be exercised where it is likely to give a competitive advantage to the person who benefits from the relief.

Recommendation – Part IIIA – Prudential Supervision of Authorised General Insurers

We recommend that the general insurance advisory panel should be given a statutory basis.

Recommendation – Division 2 – Part IV - APRA may give directions to comply with Prudential Standards and Prudential Regulations

We believe care needs to be taken in relation to the power to give directions that the interests of third parties are adequately protected.

Recommendation – Part IV – Auditors and Actuaries

A proper balance between the responsibility of the Board and the whistle blowing activities of an auditor and/or actuary is met by requiring the auditor and/or valuation actuary to report a matter to the Board which may involve a breach or a potential beach of prudential requirements or where there is a material risk to policy holders. The obligation to report to APRA should then arise if, in the view of the reporting body, there is a failure by the Board to take appropriate step.

Recommendation –Division 5 – Part IV– Accounts

The situation that arises where an insurer determines not to adopt the liability valuation standards, needs to be clarified. There should be no inference of non-compliance rather what should occur is the alternate standard needs to be reported to APRA and the alternate standards needs to be fully disclosed in the Financial Reports of the company.\(^{15}\)

Government rationale for Bill

The Government through the Second Reading Speech and Explanatory Memorandum to the Bill advances a number of rationale for the amendments to the Insurance Act 1997, including:

- to place Australia at the forefront of international best practice\(^{16}\)
- bring the general insurance regime into line with changes that have already occurred in authorised deposit taking institutions and life insurers in Australia\(^{17}\)
- the current Insurance Act is widely perceived to be blunt and unresponsive in the face of market development that have transformed the financial sector over recent years\(^{18}\)
– to make it clear that the purpose of the Insurance Act is to protect policy holders and other beneficiaries of general insurance policies\(^{19}\)

– to minimise compliance costs and restrictions on competition where these cannot be justified on cost/benefit grounds,\(^{20}\) and

– to ensure that the general insurance regime is more consistent with other supervisory regimes administered by APRA.\(^{21}\)

Media comment

Much of the media comment relating to the introduction of this Bill has related to the collapse of HIH Insurance Limited (HIH).\(^ {22}\)

For example, it is reported in The Canberra Times of 10 August 2001 that up to 50 general insurers will be swallowed up or forced to shut if they cannot meet tougher standards for the general insurance industry after the HIH collapse. The Minister for Financial Services, the Hon. Joe Hockey is reported in the same articles as stating:

> It was decided to bring forward these particular amendments in response to APRA’s dealing with HIH.

The General Insurance Reform Bills unabashedly are going to reduce the number of general insurers in Australia.

We are doing that because there are a number of very small insurers that will find it very difficult to cope with the new global environment for financial services.

The companies have until July 1, 2004, to merge or be taken over if they cannot raise enough capital to operate under the new regime.

The Chief Executive of APRA is reported in The Financial Review of 29 June 2001 as stating that:

> The new regime could have prevented HIH’s collapse by providing an earlier and clearer warning of the company’s financial problems.

The Australian managing director of Royal & Sun Alliance Limited is reported in The Sydney Morning Herald of 16 May 2001 as stating that:

> Earlier implementation [of the amendments proposed by this Bill and new prudential standards] might see a shake-out among smaller players. … On the basis of the new capital standards, we already comply with those. If they are bringing it forward we’ll need to change our systems a little earlier.

The Chief Executive of APRA is reported in The Age of 15 May 2001 as stating that:

> … the overhaul was designed to protect policy-holders without imposing unnecessary costs and red tape on insurers.

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These proposals, when implemented, will give Australia a much more effective supervisory system for general insurers and will encourage an upgrading of the industry’s risk management and governance practices.

… under the old regulatory regime there was also too much room for companies to choose their own approach in valuing insurance liabilities, from very conservative to very optimistic.

The Governor of the Reserve Bank, Ian Macfarlane, is reported in the same article as stating:

… the authority [APRA] had been trying to push the reforms through since mid-1999 but had faced considerable opposition from the industry.

If there is one good thing that has come out of HIH it is that the opposition has finally retreated and we are going to see some actions pretty soon.

Main Provisions

Object of Act

An object section (new section 2A) is inserted in the Insurance Act 1973 (the Insurance Act) by item 1 of Schedule 1. The provision provides that the main object of the Insurance Act is to protect the interests of policy holders and prospective policy holders under insurance policies (issued by general insurers and Lloyd’s underwriters) consistent with the continued development of a viable, competitive and innovative insurance industry.

The new section also states how the main object of the Insurance Act is to be achieved, namely:

- restricting who can carry on insurance business by requiring general insurers, and the directors and senior management of general insurers, to meet certain suitability requirements
- imposing primary responsibility for protecting policyholders on directors and senior management of general insurers
- imposing on general insurers requirements to promote prudent management of their insurance business, and
- providing for the prudential supervision of general insurers by APRA.
Prudential matters

A new definition of “prudential matters” is inserted in the Insurance Act by item 12 of Schedule 1. A prudential matter, in relation to a general insurer, authorised non-operating holding company (NOHC) or a subsidiary of a general insurer or authorised NOHC is defined to mean:

- the conduct by the insurer, NOHC or subsidiary of any of its affairs in such a way as:
  - to keep itself in a sound financial position; or
  - not to cause or promote instability in the Australian financial system; or
- the conduct by the insurer, NOHC or subsidiary of any of its affairs with integrity, prudence and professional skill.

Application of Insurance Act

A new subsection 5(2), dealing with the application of the Insurance Act, is substituted in the Insurance Act by item 20 of Schedule 1 of the Bill. New subsection 5(2) provides that the Insurance Act does not apply to insurance business carried on by:

- the Commonwealth and its territories
- a prescribed corporation, or
- a corporation, being an insurance business prescribed by the regulations.

Power of APRA to determine provisions do not apply

New sections 7 and 7A, dealing with determinations of APRA that provisions of the Insurance Act do not apply, are inserted in the Insurance Act by item 21 of Schedule 1 of the Bill. APRA is accorded power under new section 7 to determine that all or specified provisions of the Insurance Act do not apply to a person while the determination is in force. A determination may apply to an individual or class of persons, specify the period during which the determination is to last and be made subject to specified conditions. Determinations must be published in the Commonwealth Gazette. Additionally, APRA may vary or revoke a determination through a determination published in the Commonwealth Gazette.

It will be an offence, punishable by a maximum fine of 60 penalty units ($6600) for an individual and 300 penalty units for a corporation ($33 000), where a person does or fails to do an act which results in a breach of a new section 7 condition.

Authorisation to carry on insurance business

A new Part III (new sections 9-31), dealing with authorisation to carry on insurance business, is substituted in the Insurance Act by item 22 of Schedule 1.
New section 9 makes it an offence for a person to carry on insurance business, punishable by a maximum fine of 60 penalty units ($6600), if the person is not a corporation or a Lloyd’s underwriter, and there is no section 7 APRA determination in force that this section does not apply. [Note: New section 128A, which is inserted in the Insurance Act by item 68 of Schedule 1, provides APRA with the option of giving a person written notice of its belief that he/she has done an act or failed to do an act in circumstances that give rise to an offence. The new section makes the offence applicable from the day the notice is received and for each subsequent day the breach continues. Thus, the penalty will accrue for every day the offence continues.]

New section 10 makes it an offence, punishable by a maximum fine of 300 penalty units ($33 000), for a corporation or Lloyd’s underwriter to carry on insurance business in Australia without authorisation and there is no section 7 APRA determination in force that this section does not apply.

New section 12 provides that a corporation may apply to APRA for an authorisation to carry on insurance business in Australia and grants APRA the power to authorise an applicant to carry on such business. APRA may refuse an application if the applicant is a subsidiary of a NOHC that is not an authorised NOHC. A decision by APRA to refuse an authorisation is subject to Administrative Appeals Tribunal review under Part VI of the Insurance Act. [Note: A corporation that is authorised under new section 12 is defined by new section 11 to be general insurer.]

APRA is accorded power under new section 13 to impose certain conditions on any authorisation, or vary or revoke conditions imposed on an insurer’s authorisation. Conditions must relate to prudential matters. Additionally, APRA may make an authorisation conditional on a corporation, of which the insurer is a subsidiary, being an authorised NOHC.

It will be an offence punishable by a maximum fine of 300 penalty units ($33 000) under new section 14 for a general insurer to do or fail to do an act which results in a breach of a new section 13 condition unless there is a new section 7 APRA determination in force that this section does not apply.

New section 15 deals with the circumstances under which APRA may revoke a general insurer’s authorisation. The circumstances include:

- a failure to comply with a requirement of the Insurance Act
- where it would be contrary to the national interest for the authorisation to remain in force
- a failure to pay a statutory amount of levy, late penalty or charge
- where the insurer is insolvent and is unlikely to return to solvency within a reasonable period of time, or

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• where the insurer has inadequate capital and is unlikely to have adequate capital within a reasonable period of time.

Revocation under the circumstances specified in **new section 15** require the Treasurer’s approval.

APRA must revoke a general insurer’s authorisation if:

• the insurer asks APRA; and

• APRA is satisfied that the insurer has no liabilities in respect of insurance business carried on by it in Australia, and the revocation would not be contrary to the national interest (**new section 16**).

APRA is accorded power under **new section 17** to direct a general insurer to assign its liabilities to one or more other general insurers where APRA considers that it would revoke the general’s insurer’s authorisation under **new section 15** if the general insurer had no liabilities in respect of its Australian insurance business.

Assignment of liabilities may include the assignment of any rights or benefits in connection with contracts of insurance.

**New section 17** also allows a general insurer who has asked APRA for a revocation to ask APRA to approve an assignment of its insurance business liabilities. APRA may only approve an assignment of a general insurer’s liabilities where satisfied of certain matters, including whether the assignment is in:

• the national interest

• the interests of the insurer’s policyholders, and

• any other matter APRA considers relevant.

APRA authorisation to be a NOHC

**New sections 18-23** deal with the authorisation of a company as a non-operating holding company (NOHC). A corporation is a NOHC in relation to another corporation (the first corporation) if the first corporation is a subsidiary of the corporation and the corporation undertakes no business other than the ownership or control of other corporations (**item 9** of **Schedule 1**).

**New section 18** provides that a corporation may apply to APRA for authorisation to operate as an NOHC and grants APRA the power to so authorise an applicant if it considers it appropriate. An authorisation operates as an authorisation in relation to the corporation and any general insurers that are subsidiaries of the corporation. A decision by APRA to refuse an NOHC authorisation is subject to Administrative Appeals Tribunal review under Part V of the Insurance Act.
APRA is accorded power under **new section 19** to impose certain conditions on any NOHC authorisation, or vary or revoke conditions imposed on an insurer’s authorisation. Conditions must relate to prudential matters. Additionally, APRA may make an authorisation conditional on a corporation, of which the insurer is a subsidiary, being an authorised NOHC.

The effect of **new sections 20-22** are substantially the same effect as new sections 14-17 (see above), except that they apply to NOHC authorisations.

**New section 23** allows APRA to publish, at whichever time it thinks necessary, a list of authorised NOHCs. Publication of the list can be in any form APRA thinks appropriate.

**Persons disqualified from acting as general insurers**

**New section 24** is an offence provision relating to disqualified persons. The term disqualified person is defined by **new section 25** to include:

- a person convicted of an offence against or arising out of an Australian or foreign law if that offence concerned dishonest conduct or conduct relating to a financial sector company

- a person who has been or becomes bankrupt

- a person who has applied to take the benefit of a law for relief of bankrupt or insolvent debtors, or

- a person who has compounded with his or her creditors.\(^{23}\)

Under **new section 24** a disqualified person must not be, or act as:

- a director or senior manager of a general insurer (other than a foreign general insurer)

- a director or senior manager of an authorised NOHC, or

- a senior manager or agent of a foreign general insurer.

Where a disqualified person is, or acts in, one of the above positions he/she will have committed a strict liability offence attracting a maximum fine of 60 penalty units ($6600 or $27,500 for a corporation) and also be subject to a maximum term of imprisonment of two years. The offence attracting a term of imprisonment is not one of strict liability.

Despite the effect of **new section 25**, APRA under **new section 26** may determine a person is not a disqualified person. APRA may do this on its own initiative or on application of the disqualified person. However, APRA may only make such a determination if it is satisfied that the person is highly unlikely to be a prudential risk to any general insurer or authorised NOHC. An APRA refusal of an application to not be
classed as a disqualified person is subject to review by the AAT under Part VI of the
Insurance Act.

New section 27 provides that APRA may direct that a general insurer or authorised
NOHC remove a person who is:

- a director or senior manager of a general insurer (other than a foreign general insurer)
- a director or senior manager of an authorised NOHC, or
- a senior manager or agent of a foreign general insurer.

where satisfied the person is a disqualified person, or does not meet one or more of the
criteria for fitness and propriety set out in the prudential standards.

It will be an offence punishable by a maximum fine of 200 penalty units ($22 000) under
new section 28 if:

- or general insurer does not hold assets in Australia (excluding goodwill and any other
  amount excluded by the prudential standards) equal to or more than the total amount of
  its liabilities in Australia
- APRA has not authorised the insurer to hold assets of a lesser value, and
- there is no APRA determination operating exempting a particular insurer from the
  operation of this section.

Prudential supervision and monitoring

APRA is given the power under new section 32 to determine prudential standards. These
standards must be complied with by all general insurers, all authorised NOHCs, the
subsidiaries of general insurers or authorised NOHCs, or a specified class of general
insurers, authorised NOHCs or subsidiaries of general insurers or authorised NOHCs.

In making a prudential standard, APRA must have regard to good commercial practice and
the cost in complying with the requirements of a standard.

An APRA determination of a prudential standard, variation or revocation of a prudential
standard, is a disallowable instrument for the purposes of section 46A of the Acts
Interpretation Act 1901 and consequently subject to disallowance by either house of the
Australian Parliament.

New section 36 provides APRA with the power to direct a general insurer, authorised
NOHC or subsidiary of a general insurer or authorised NOHC, where satisfied they have
breached a prudential standard, or are likely to, to comply with all or a part of the standard
within a specified time. A direction must be complied with despite anything in a
corporations constitution or any contract or arrangement to which it is a party.
Failure to comply with a new section 36 direction will constitute an offence punishable by a maximum fine of 60 penalty units ($6600) (New section 37).

APRA is accorded the specific monitoring functions by new section 38 of:

- collecting and analysing information on prudential matters concerning general insurers, authorised NOHCs and the subsidiaries of general insurers and authorised NOHCs
- encouraging and promoting the carrying out of sound practices in relation to prudential matters by general insurers, authorised NOHCs and the subsidiaries of general insurers and authorised NOHCs, and
- evaluating the effectiveness and carrying out of those practices.

Rules affecting auditors and actuaries of insurers

New sections 39-49Q, dealing with role of auditors and actuaries in relation to insurers, are inserted in the Insurance Act by item 23 of Schedule 1. The key requirements imposed on insurers, auditors and actuaries by the new sections include:

- a general insurer must have an APRA approved auditor and actuary (new section 39);
- APRA can only approve an appointment as a general insurer’s auditor or actuary if satisfied that the person meets the eligibility criteria set out in the prudential standards and there is no determination current disqualifying the person from holding the appointment (new section 40) [Note: An APRA refusal to approve a person’s appointment is subject to review by the Administrative Appeals Tribunal under Part VI of the Insurance Act]
- auditors and actuaries must comply with the prudential standards when performing his/her duties or exercising his/her powers (new section 41)
- APRA may revoke an approval of an appointment as an auditor or actuary where satisfied the person has failed to perform adequately and properly the functions and duties of the appointment under the Insurance Act or the prudential standards, or does not meet one or more of the criteria for fitness and propriety set out in the prudential standards (new section 42) [Note: An APRA refusal to approve a person’s appointment is subject to review by the Administrative Appeals Tribunal under Part VI of the Insurance Act]
- APRA may determine that a person is disqualified from holding any appointment as an auditor or actuary of a general insurer where it determines he/she has failed to perform adequately and properly the functions and duties of such an appointment under the Insurance Act or the prudential standards, or does not meet one or more of the criteria for fitness and propriety set out in the prudential standards (new section 44) [Note: A
disqualification is subject to review by the Administrative Appeals Tribunal under Part VI of the Insurance Act]

- APRA may determine that one or more general insurers are exempt from the requirement to appoint an actuary (new section 47)

- where directed to by APRA, require a person who is or was an auditor or actuary of a general insurer, authorised NOHC, or a subsidiary of a general insurer or authorised NOHC, is to provide information on matters relating to those bodies where APRA considers that the information will assist it in performing its functions under the Insurance Act (new section 49). [Note: Failure to provide information will constitute an offence punishable by a maximum fine of 100 penalty units ($11,100) or a maximum term of imprisonment of 6 months, or both. Additionally, a failure to provide information will constitute a strict liability offence attracting a maximum fine of 60 penalty units ($6,600)]

- an approved auditor or actuary must inform APRA where he/she has reasonable grounds for believing that:
  - the insurer, NOHC or subsidiary is insolvent, or there is a significant risk that it will become insolvent
  - the insurer, NOHC or subsidiary has failed to comply with the prudential standards or a condition of its authorisation
  - the insurer, NOHC or subsidiary has failed to comply with a requirement or direction under the Insurance Act or Financial Sector (Collection of Data) Act 2001, and
  - an existing or proposed state of affairs may materially prejudice the interests of the insurer’s policy holders, or the policyholders of any general insurer who is a subsidiary of an NOHC [Note; Failure to provide information will constitute an offence punishable by a maximum fine of 100 penalty units ($11,100) or a maximum term of imprisonment of 6 months, or both. Additionally, a failure to provide information will constitute a strict liability offence attracting a maximum fine of 60 penalty units ($6,600)] (new section 49A).

- an auditor or actuary who provides information to APRA in good faith and without negligence will not be subject to any action, claim, demand, or liability to any other person in respect to that information (new section 49C)

- that APRA can require a general insurer to appoint an independent actuary to investigate all or part of the insurer’s liabilities and produce a written report (new section 49E)
• will specify that the role of an auditor appointed under new section 39 by a general insurer be to audit the insurer’s yearly statutory accounts, perform the functions of an auditor set out in the prudential standards and prepare any reports required by the prudential standards (new section 49J), and

• subject to the Treasurer’s approval, that APRA can direct a general insurer to provide, or further provide, its accounts a specified amount, or an amount determined in a specified way, in respect of its liabilities (new section 49M) [Note: It will be an offence punishable by a maximum fine of 60 penalty units ($6600) for a general insurer to breach a section 49M direction].

Where it appears to APRA that an authorised insurer is or is likely to become unable to meet its liabilities it may, under subsection 51(1) of the Insurance Act:

• direct the insurer to provide, within a specified period of not less than seven days, any information about its affairs as APRA specifies (paragraph 51(1)(a))

• direct the insurer, with the Treasurer’s approval, not to dispose of or otherwise deal with or remove from Australia, during a specified period not greater than six months, any asset in Australia which APRA specifies (paragraph 51(1)(b)), or

• direct the insurer, with the Treasurer’s approval, to deal with any asset, or any specified asset, of the corporation on the terms and conditions specified in the notice (paragraph 51(1)(b)).

The scope of APRA’s powers under section 51 of the Insurance Act are extended by items 30 and 31 of Schedule 1 to authorised NOHCs and situations where a general insurer or authorised NOHC has contravened or failed to comply with a provision of the Insurance Act or a condition or direction applicable under the Insurance Act.

A new section 128A is inserted in the Insurance Act by item 68 of Schedule 1 of the Bill and provides APRA with the power to give a person written notice that it believes he/she has done an act or failed to do an act in circumstances that gave rise to an offence under new sections 7A, 9, 10, 14, 20, 28, 37 or 49P. The effect of such a notice is that the alleged breach will be taken to have been a breach from the day the notice is received and for each subsequent day the breach continues.

Transitional provisions

The effect of item 3 of Schedule 2 of the Bill is to allow general insurers and APRA to appoint and approve auditors and actuaries prior to the commencement of this Bill. Item 3 allows for such appointments and approval to take place from Royal Assent. An appointment or approval given before the commencement of this Bill will be taken to have effect on the day specified by APRA. That day must not be before the commencement of the Bill.
APRA is accorded power by item 4 of Schedule 2 to determine that all or specified provisions of the existing Insurance Act continue to apply to a person or class of persons for a specified period during the transition period (i.e. the period starting on the commencement and ending 2 years after the commencement).

APRA is accorded power by item 5 of Schedule 2 to determine that all or specified provisions of the Insurance Act as amended by this Bill do not apply to a person or class of persons for a specified period during the transition period.

Item 10 of Schedule 2 provides APRA with power during the transition period to give directions to persons to whom some or all of the existing Insurance Act applies, or to person to whom some or all of the Insurance Act as amended by this Bill applies.

Concluding Comments

The most important reform to the current regime proposed by the Bill is the grant to APRA of power to make, vary and revoke prudential standards. These standards will be subordinate to the Insurance Act 1973 and disallowable instruments. [Core regulatory powers under the current Insurance Act are outlined in the Background to this Digest] As such, the prudential standards will be subject to disallowance by the Australian Parliament.

The Government has indicated that it is proposed that there will be four prudential standards on liability valuation, capital adequacy, reinsurance arrangements and risk management.24

The proposed new prudential standards will see minimum statutory capital requirements increase for most insurers and the minimum level of capital for general insurers will be raised from $2 million to $5 million.25

The Government has also indicated in relation to prudential standards that risk weighted capital adequacy, similar to that used in banking regulation will be introduced, allowing different insurance product lines to require different amounts of capital to be held by the insurer.26

As noted in the Government’s Explanatory Memorandum to the Bill, a long and wide ranging consultative process has been undertaken with general insurers and industry bodies in relation to the amendments proposed by this Bill and the forthcoming prudential standards. In addition to issuing discussion papers on the proposed form of this Bill and the key aspects of the proposals for general insurance reform, APRA has issued several drafts of the proposed prudential standards. These draft standards can be viewed at: http://www.apra.gov.au/policy/general_insurance_discussion_papers/default.htm.
Endnotes

4. ibid., at p. 4,702–4,704.
5. Each State and Territory is accorded power under the Constitution to write insurance. The State and Territory Governments have established statutory insurance corporations. These bodies derive all their powers from an Act of the relevant State or Territory Government. A number of State insurance offices have been privatised. For example, the NSW State Government Insurance Office was privatised in 1992. Once a State or Territory insurance office has been privatised it no longer comes under the jurisdiction of the relevant State or Territory government, it becomes subject to the Commonwealth’s legislation.
10. ibid.
17. ibid.
19. ibid.
20 ibid.
21 ibid.
23 To compound is to settle a debt due and owing by agreeing to accept a lesser amount.
25 ibid.
26 ibid.