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24 November 2005

Regulation Taskforce
PO Box 282,
Belconnen ACT 2616

Dear Sirs

QBE response to Regulation Taskforce

I refer to your circular dated 25 October 2005 calling for submissions on reducing the regulatory burden on business.

Further to the response provided to you by the Insurance Council of Australia (ICA) with QBE's input, QBE's response on particular issues affecting QBE is set out at Attachment A.

We welcome the opportunity to assist you in identifying efficiency gains with practical suggestions to improve the operation of regulation in Australia, particularly those affecting the financial sector.

QBE's business is affected by a broad range of regulation both in Australia and in over 40 countries in which it operates. QBE's overseas operations represent $7.5 billion of premium income or 75% of its worldwide business.

As with other large organisations, QBE believes that part of its role is to encourage innovation in the way we conduct our business, by continuing to take measured risks and pursuing commercial opportunities that challenge our business and provide further opportunities for growth, both locally and overseas. By doing so, we help to create further employment opportunities, generate significant tax revenues and continue to pay dividends to our shareholders.

QBE supports regulatory reform that is proportionate, well targeted and encourages the promotion of a stable and robust financial services industry in Australia. However, QBE is concerned that much of the recent regulation is excessive and falls well short of achieving that objective. In fact it is likely to have the opposite effect by directing the attention of company directors to look for things that are wrong and thereby make companies more compliance focussed and risk averse. Ultimately, this significantly increases costs and encourages the proliferation of non regulated products in the Australian market place, which is evidenced by the growing number of direct offshore foreign insurers writing Australian risks, particularly in the past 2 years.

As a general insurance group, APRA is our main regulator. In its first round of regulatory reforms introduced in 2002, APRA made significant improvements to the prudential supervision of general insurance in Australia. The first was to introduce a risk based capital requirement that included a requirement, for significant prudential margins to be held by all insurance companies. The regime also introduced standards in respect of risk

and reinsurance management. The situation in which HIH found itself prior to its collapse would be extremely unlikely under the prudential requirements of the reforms introduced in 2002. These changes were necessary and had the full support of QBE. In fact, QBE believes that no other regulation was necessary other than the fit and proper requirements.

However, since 2002, APRA has proposed a number of unnecessary changes to the prudential regime that the insurance industry considered to be very prescriptive in nature as well as overlapping with other regulators, including ASIC and ASX.

It is important to note that, in the past six weeks, APRA appears to have heard the message from industry and others about effective regulation vs over regulation and has moved back from more prescriptive standards to a more principles based approach. Some of the detailed changes are not yet available from APRA and there is still much detail to be worked through. However, QBE is encouraged at APRA's apparent change of direction in respect of prudential supervision.

There are a number of areas of concern for QBE and these are set out in our response in Attachment A. Some of QBE's concerns may disappear as a result of APRA's change of direction but are included until the final outcome is clearer. There are three issues that I particularly wish to draw to your attention.

Increasing compliance costs

The first is the increase in compliance costs for Australian financial services companies in recent years. QBE estimates that the group now spends in excess of $60 million per annum in compliance costs. Further, we have estimated that APRA's recent proposals would add between $7.5 and $10 million to our compliance costs.

While QBE understands and accepts that all regulation has a cost, our key concern is that these costs are ultimately borne by policyholders with little additional benefit to them in terms of increased protection. There is also no quantifiable return on investment or delivery of improved business benefits to QBE or to its shareholders. Even with the recent change of direction signalled by APRA, the proposed changes in respect of actuarial peer review and financial condition reports are likely to increase our compliance costs by $2.5 to $5 million.

Regulation of overseas operations

The second is APRA's seeming unwillingness to recognise that QBE's general insurance companies in Australia can be effectively ringfenced from the impact of our overseas operations. Much of what APRA is currently doing and proposing to do increases its regulation of our overseas operations that do not affect Australian policyholders of QBE and is in addition to the local regulation with which QBE must already comply.

Our overseas operations are already subject to the requirements of local regulators and much of what APRA is doing is pure duplication. In this regard, I include at Attachment B, C and L APRA's detailed agendas for overseas visits to the UK (in May 2004) and the US (proposed for June 2006). QBE received reports from APRA following the visits in 2004 which raised no major concerns, copies of which are available to the Taskforce upon request. QBE in the USA recently had a six month audit by the Pennsylvania Insurance Department with no major issues arising from that audit.

QBE has made recommendations to APRA on the minimum requirements we feel necessary for the regulation of a group domiciled in Australia with overseas operations, such as ours.

Uneven playing field for insurers in Australia

The third issue relates to Treasury's failure to date to implement the recommendations of the HIH Royal Commission in respect of state and territory regulation, taxation of the general insurance industry and a policyholder support scheme (recommendations 49 to 61). These items, and particularly recommendations 40 to 60, would go a long way to achieving a level playing field and alleviating some of the regulatory burden on Australian general insurers.

The proposed regulation of overseas operations and the uneven playing field for insurers domiciled in Australia are of such significant concern to QBE that, if we cannot agree on a more sensible level of prudential supervision that still achieves the government's, APRA's and QBE's objectives, our board will consider moving QBE's domicile offshore. This would of course involve a loss of employment and tax revenues for Australia.

While APRA's proposed reforms may place it in the position of leading edge regulatory reforms when compared with other overseas regulators, we believe APRA must remember that their main priorities are to protect Australian policyholders, and to ensure that the regulatory framework they put in place will continue to facilitate a robust Australian financial services industry, in order to remain relevant.

Financial services reforms

Further to the issues detailed above, I also draw your attention to the Financial Services Reforms (FSR) which have been implemented over the past two years. Given the well established consumer focussed legislation (i.e. *Insurance Contracts Act, 1984*) and industry initiatives (i.e. Insurance Enquiries and Complaints Panel) that were operating effectively prior to the introduction of FSR, it is unfortunate such reforms were imposed on the general insurance industry without a clear understanding of the specialised nature of the industry and the significant cost and complexity that these reforms placed on general insurers and consumers.

QBE's implementation costs for FSR prior to July 2004 were $7 million. We estimate that the continuing FSR compliance costs will be at least $2.5 million per annum, due to the ongoing costs of maintaining a large number of authorised representatives, regular updating of product documents and other regulatory amendments.

Finally, there are other matters we have previously raised with APRA and Treasury and these are included as Attachments B – M as set out below.

Description of correspondence:

- APRA's draft agenda dated 27 April 2004 for prudential consultation with QBE's European Company Operations (Attachment B)
- APRA's draft agenda dated 27 April 2004 for prudential consultation with Limit Underwriting Limited (Attachment C)
- Letter from QBE to the Federal Treasurer dated 19 May 2005 in relation to Direct Offshore Foreign Insurers and the recommendations contained in the Pott's Review (Attachment D)
- Letter of reply from the Minister for Revenue and Assistant Treasurer, The Hon Mal Brough dated 11 July 2005 in relation to QBE's letter to the Federal Treasurer dated 19 May 2005 (Attachment E)
- Letter from QBE to Mr G Brunner, General Manager Policy, Research and Statistics, APRA dated 29 July 2005 attaching QBE's responses to APRA's Stage 2 reforms on:

    a. Risk and Financial Management (released 3 May 2005); and

b. Governance (released 16 May 2005) (Attachment F)

- Letter from John Cloney, QBE Group Chairman to Dr John Laker, APRA Chairman dated 24 August 2005 in relation to the Proposed APRA Prudential Standards and Guidance Notes for General Insurers (Attachment G). **This document is confidential and marked "Commercial in Confidence"**.
- Letter from QBE to Senator Grant Chapman, Chairman, Parliamentary Joint Committee of Corporations and Financial Services dated 29 September 2005 in relation to APRA's stage 2 reforms (Attachment H)
- Letter from QBE to Mr G Brunner, General Manager Policy, Research and Statistics, APRA dated 19 October 2005 in relation to APRA's prudential approach to adoption of IFRS –2 – Tier 1 Capital and Securitisation released 31 August 2005 (Attachment I)
- Letter from QBE to Mr S Somogyi, APRA Commissioner dated 24 October 2005 attaching QBE's response to APRA's stage 2 reforms on prudential supervision of corporate groups involving authorised general insurers (Attachment J)
- Letter of reply from Senator Grant Chapman dated 25 October 2005 to QBE's letter of 29 September 2005 (Attachment K)
- APRA's draft agenda dated 9 November 2005 for prudential consultation with QBE's America's Operations in June 2006 (Attachment L)
- QBE's submission to the Financial Sector Advisory Council's review of Financial Sector Regulation dated 16 November 2005 (Attachment M)

QBE would be pleased to assist with any further information you may require. If you have any questions or need further information, please call Gayle Tollifson on (02) 9375 4102 or me.

Yours faithfully

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cc Gayle Tollifson

TABLE OF CONTENTS

ISSUE 1. IMPACT OF FINANCIAL SERVICES REFORMS (FSR)

QBE acknowledges that Treasury and ASIC are making attempts to refine the FSR legislation in order to reduce its complexity and regulatory burden, both for industry and consumers. However, there are still a number of examples where FSR regulation creates an unnecessary administrative burden on insurers with little benefit to either the insurer or the insured. We believe these matters require attention, but are not being addressed in the current refinements.

1.1 Requirement to lodge an FS53 'In use notice' for every Product Disclosure Statement (PDS) and Supplementary PDS (SPDS)

This notice is required to be lodged with ASIC within 5 days of the first time the PDS or SPDS is likely to have been issued. That is, lodgment can only occur after release of the PDS or SPDS and must be within 5 days from that date. The date on the PDS or SPDS must be the "Prepared Date". The issues include:

(a) general insurers tend to have a large number of PDS documents in circulation at any one time. QBE has approximately 500.

(b) it is often the case that the release of a new PDS will be from a particular date. A number of PDS documents will be released at this time. QBE has at times released up to 85 new PDS documents from a particular date.

(c) the lodgment documents are not available on-line, so each one must be completed, printed, signed and then sent by mail to ASIC.

(d) the FS53 forms were previously 6 pages long and are now 12 pages long due to the additional information required for superannuation products. Superannuation is a business not conducted by QBE. The items required to be completed by a general insurer would only require a maximum of 2 pages.

(e) the reference number provided by the insurer is not recorded by ASIC for their accounting records. Therefore, reconciliation of hundreds of items needs to be completed by first reviewing the scanned document (once it is available) to find the ASIC created reference number, then matching these numbers to the account provided by ASIC.

However, the requirement to lodge FS53 in use notices for general insurers does not provide greater consumer protection:

(f) the *Insurance Contracts Act 1984* provides consumer protection as it establishes the rules that have been in place for many years to protect the insured. This Act is more favourable to insureds than other insurance laws overseas, compare English common law which is insurer friendly.

(g) general insurers had to retain copies of each policy version issued until all claims payable under that particular policy would have occurred, been notified and resolved.

(h) the current paper lodgment is time consuming and the information collected mostly meaningless for general insurance products.

(i) reconciliation of many individual items is time consuming and difficult due to the nature of the ASIC accounting system.

If lodgment remains a requirement, then an online form limited to those fields appropriate to general insurance products, with an online created reference number for use in reconciliation processes, is needed.

1.2 Recommendation to lessen administrative burden of the "in use notice"

QBE does not see any benefit in having to lodge an "in use" notice. As the PDS and SPDS form part of the contract of insurance, an insurer will always need to retain copies so that claims can be

determined according to the particular policy that the insured had purchased. However, the following would provide administrative relief:

(a) create an FS53 form specifically for use by general insurers.

(b) enable this form to be lodged on-line, with a reference number created by ASIC's system that would be recorded on the Tax Invoice created to facilitate payment.

(c) allow lodgment in advance of any estimated "first issue" date.

1.3 Requirement to nominate Responsible Officers (ASIC Policy Statement 164) and Responsible Persons (APRA – Fit and Proper)

QBE believes the duplication which exists between the requirement to nominate responsible officers under ASIC's Policy Statement 164 (PS 164), and responsible persons under APRA's draft Fit and Proper prudential standard GPS 520, creates an unnecessary compliance burden on insurers and must be resolved.

Currently, an APRA regulated entity that also holds an Australian Financial Services License is required to nominate a number of officers as responsible officers or responsible persons, depending upon the regulator with which it is complying.

(a) ASIC requires initial notification and then notice of removal or addition within 10 days.

(b) APRA has only issued draft requirements; however, its current draft standard requires a Fit and Proper Policy to be put in place by the Board of the regulated entity and notification provisions which are similar to those in ASIC's PS 164 to be followed.

Duplication and a lack of clarity arises due to the differing definitions applying to each set of requirements.

PS 164 relies of the definition of "responsible officer" under sec 9 of the Corporation Act 2001 –

> "responsible officer, in relation to a body corporate that applies for an Australian financial services licence, means an officer of the body who would perform duties in connection with the holding of the licence."

However, this definition refers to an "*officer of the body who would perform duties in connection with the holding of the licence*", from which it can be inferred is someone at a senior level within the company or who has decision making authority to affect the company's business.

Section 9 of the Corporations Act defines "officer" to include:

(a) a director or secretary of the corporation; or

(b) a person:
- who makes, or participates in making, decisions that affect the whole, or a substantial part, of the business of the corporation; or
- who has the capacity to affect significantly the corporation's financial standing;……

The definition of "responsible person" under APRA draft prudential standard GPS 520 includes:

(c) a director of the regulated financial institution; and

(d) a person who exercises any senior management responsibilities for the regulated institution (senior manager).

Section 4 of GPS 520 defines "senior management responsibilities" to mean any relevant activities that may materially affect the whole or a substantial part of the regulated institution's business or its financial standing."

Therefore, it is clear that with both APRA's draft standard GPS 520 and ASIC's PS 164, an insurer which is regulated by APRA and which also holds an Australian Financial Services License issued by

ASIC has the unnecessary compliance burden of meeting two sets of fit and proper requirements for essentially the same persons, but with no added benefit to the insurer or its policyholders.

1.4 Recommendation to lessen the compliance burden of Fit and Proper Requirements

(a) Remove the need for an APRA regulated entity that has nominated its "responsible persons" to APRA to be required to nominate responsible officers to ASIC in accordance with ASIC PS 164.

(b) There should be no requirement to provide a restatement about individuals to APRA on an annual basis.

(c) A statement by the Board under GPS 520 that the responsible person of the entity is "fit and proper", should also meet all requirements in terms of organisational competency under PS164.

1.5 Requirement to lodge annual financial statements and auditor's report with ASIC

A further example of duplication from FSR arises due to the requirements of section 989B of the Corporations Act 2001, and regulations 7.8.13 and 7.8.14 of the Corporations Regulations 2001, which provide that a financial services licensee must prepare and lodge with ASIC an annual profit and loss statement and balance sheet, both of which must contain an auditor's report prepared in accordance with the Corporations Regulations.

Currently, a listed public company is required to provide audited financial statements to ASIC and ASX. An entity supervised by APRA must lodge various financial and auditor statements.

As such, this means that in addition to these existing reporting requirements, a listed entity that is regulated by APRA and which holds an Australian Financial Services License must also lodge further financial statements and auditors reports with ASIC.

1.6 Recommendation to remove compliance burden of ASIC's licensee financial statements

QBE believes it should not be required to incur additional costs by having to prepare further financial statements and audit reports for information which is already available to ASIC and which provides no further protection or benefit to policyholders, shareholders or other stakeholders.

We recommend that the regulators rationalise the required financial reporting to one set of reports that can be provided to any regulator, along with a single auditors' report that covers off all requirements. Removal of this requirement on Australian financial services licensees will be in keeping with the current efforts to refine FSR and remove its complexity and compliance burden, both for insurers and policyholders.

ISSUE 2. APRA'S PROPOSED EXTRATERRITORIAL JURISDICTION

2.1 Application of APRA's prudential standards to QBE Group's overseas subsidiaries

As a global organisation with numerous subsidiaries located overseas, QBE is subject to multiple regulatory regimes. It is apparent from APRA's proposed regulatory reforms (particularly its draft discussion paper on prudential supervision of corporate groups involving general insurers) that APRA is seeking to extend its jurisdiction beyond QBE's Australian authorised entities to its subsidiaries located overseas. APRA's prudential standards are in effect regulations under the *Insurance Act 1973.*

If this were to occur, it would create an overlap for QBE by forcing us to comply with APRA's requirements both locally and overseas, whilst also having to meet the requirements of the local overseas regulator. This is an untenable scenario due to the significant costs of complying with two sets of overlapping, but different regulations in different jurisdictions and with little benefit to Australian policyholders.

For example, in sections 5.3 and 5.4 of APRA's discussion paper mentioned above, it states that the following prudential standard and draft prudential standards will in due course be applied at both insurer and group levels:

- GPS 222, business continuity [5.4]
- draft GPSs 510 and 511, governance [5.3]
- draft GPS 220, risk management [5.4]
- draft GPS 221, managing outsourcing arrangements [5.4]

More specifically, the:

- board of the head company will have to ensure that adequate policies, systems and controls are in place to monitor compliance with APRA's regulatory requirements on a group-wide basis [5.4];
- requirement for insurers to provide a declaration to APRA in relation to the risk management systems will be extended to apply to the head company of the group [5.4]; and
- auditor will be required to report on the effectiveness of group systems to ensure compliance with APRA's prudential requirements on a group basis and any non-compliance [5.4].

The declaration under the current prudential standard on risk management requires the boards of licensed insurers to provide an opinion that the insurer has systems in place to ensure compliance with the *Insurance Act 1973*, *Insurance Regulations 1974*, prudential standards, authorisation conditions and directions. If these requirements are extended to apply at a group level, all entities within a consolidated group will need to comply in order for the board to sign such a declaration.

A further example of APRA's intention to extend its jurisdiction to overseas entities are its visits to QBE's overseas operations. These entities are registered in their home country and subject to regulations from their home country regulator, but have to date cooperated with APRA's request for visit to their operations which involves significant time in preparing and participating in such visits. In this regard, we have included at Attachment B, C and L APRA's detailed agendas for the overseas visits to the UK (in May 2004) and the US (proposed for June 2006).

It is also worth noting that QBE received reports from APRA following the UK visits in 2004 which raised no major concerns. Copies of these reports are available to the Taskforce upon request.

2.2 Recommendation on APRA's jurisdictional limits

QBE strongly opposes APRA effectively extending the jurisdiction of Australian legislation to QBE entities outside of Australia which are already regulated by the local regulator in their home country

and which do not play any role in the operation of QBE's Australian regulated entities. These overseas entities do not need to comply with APRA's requirements, nor should they, particularly where there is no benefit or direct nexus to Australian policyholders. There are constitutional doubts on Australian legislation applying overseas. As part of international comity, the Australian Parliament should respect the laws of other countries and not seek to impose its laws overseas. There are difficult issues in Australian or overseas courts enforcing Australian laws overseas.

Section 32(1) of the *Insurance Act 1973* provides that APRA may determine prudential standards relating to prudential matters that must be complied with by:

(a) all general insurers, or

(b) all authorised non-operating holding companies (NOHCs), or

(c) the subsidiaries of general insurers or authorised NOHCs; or

(d) a specified class of general insurers, authorised NOHCs or subsidiaries of general insurers or authorised NOHCs.

The term *general insurer* is defined in s11 of the Insurance Act to mean "a body corporate that is authorised under s12 to carry on insurance business in Australia." The note contained in section 11 states that *general insurer* includes a *foreign general insurer* . Section 3(1) of the Insurance Act defines *foreign general insurer* to mean a body corporate that:

(a) is a foreign corporation within the meaning of paragraph 51(xx) of the Constitution; and

(b) is authorised to carry on insurance business in a foreign country; and

(c) is authorised under section 12 to carry on insurance business in Australia.

Therefore, in providing APRA its powers under s32(1) of the Insurance Act 1973 to determine and enforce prudential standards, we do not believe it was the intention, nor was it envisaged by the Commonwealth Parliament, that APRA's powers be extended to QBE's overseas registered entities which are already regulated in their home country, which are not foreign general insurers (by definition), and which play no role in the operation of QBE's Australian licensed entities and do not affect Australian policyholders.

We believe that as a body established by the powers of the Commonwealth of Australia, and as a matter of law, APRA does not have the jurisdictional power to enforce its regulation on such overseas entities discussed above, and any such moves by APRA to extend its powers and prudential standards to QBE's overseas entities is unnecessary and against the spirit of the legislation.

Further, if APRA's powers were to be extended to cover such overseas entities, it would result in an uneven playing field for all insurance industry participants. In particular, an extra burden is placed on those corporate groups such as QBE, which operates in over 40 countries and whose overseas operations represent $7.5 billion of premium income or 75% of its worldwide business, and are subject to separate regulation in each country.

QBE recommends that APRA's powers and the application of its prudential standards be expressly limited to those entities that are carrying on insurance business in Australia and therefore affect Australian policyholders and other local beneficiaries.

2.3 APRA's approach to supervision of corporate groups (ringfencing)

In line with our comments in section 2.1 and 2.2 above, QBE believes a sensible way for APRA to balance its prudential responsibilities with the fair interests of the entities it regulates and those of its policyholders is to allow ringfencing, whereby the assets of particular entities are held and solely used for the protection of Australian policyholders.

QBE agrees with the principle of ringfencing and the need for Australian insurers and NOHCs to be able to demonstrate that contagion risk from related entities is being appropriately managed. QBE

also agrees with the need to demonstrate that the "overall group is financially sound" through meeting APRA's capital adequacy requirements at a group level.

However, to date, there appears to be an unwillingness by APRA to recognise that QBE's general insurance companies in Australia can be effectively ringfenced from the impact of our overseas operations to the extent that APRA could focus its regulation more on the Australian operations of multi national groups, rather than their overseas subsidiaries. Further, APRA's approach to regulating corporate groups is inconsistent. The ringfencing mechanisms that are being offered to commercial groups and financial services groups that include general insurance companies are not being made available to homogenous general insurance groups like QBE, when approximately 75% of our operations are overseas. This is not rational, it discriminates against QBE relative to most of its peers in the Australian general insurance industry and puts QBE at a competitive disadvantage in Australia and overseas due to the increased cost of compliance for no benefit to Australian policyholders.

2.4 Recommendation in relation to APRA's approach (ringfencing)

APRA's proposals, if applied to international corporate groups like QBE, would result in a significant amount of regulatory duplication with the requirements of overseas regulators as well as possible conflicting requirements.

QBE believes this approach is unwarranted and that effective ringfencing of Australian regulated entities can be achieved. This would be preferable to APRA's current proposal which will merely result in duplication of regulatory requirements with little or no benefit to Australian policyholders and other beneficiaries.

We would support APRA introducing ringfencing to protect Australian policyholders and would be willing to facilitate discussion on the matter, because currently we feel general insurance groups are being discriminated against from a regulatory perspective.

ISSUE 3. AUDIT AND ACTUARIAL REPORTING AND VALUATION

QBE is concerned with the increased compliance burden and cost that will result from APRA's draft proposals relating to audit and actuarial reporting and valuation, contained in draft prudential standard GPS 310 and draft guidance notes GGN 310.1 and 310.2.

Even with the recent change of direction signalled by APRA in relation to relaxing the prescriptive nature of its draft standards for a more principles based approach, the proposed changes in respect of actuarial peer review and financial condition reports discussed below are likely to increase our compliance costs by $2.5 to $5 million.

3.1 Actuarial cost of compliance

In GPS 310 at paragraphs 13 and 58 – 65, APRA has proposed that the liability valuation report (LVR) completed by the approved actuary be subject to peer review by an external reviewing actuary. The reviewing actuary must be approved by APRA in the same manner as the approved actuary. The reviewing actuary is not required to review the proposed Financial Condition Report (FCR), except for the LVR section, should this be incorporated into the FCR.

QBE has a long standing practice of having most of its actuarial central estimates peer reviewed by an external actuary and would be happy to extend the peer review process to the LVR prepared for APRA. However, as noted below, QBE believes that this will add to the cost of compliance as the reviewing actuary will be reviewing a number of new items in addition to the central estimates. Aside from creating a further unnecessary drain on resources, it also adds compliance costs, both internally and externally, which are ultimately passed onto policyholders.

3.2 Timetable for review and cost of compliance

GPS 310 at paragraph 28 states that an approved actuary must provide the FCR and LVR to the insurer within such time as to give the board of the insurer a reasonable opportunity to:

- consider and use the FCR and the LVR in preparing the insurer's yearly statutory accounts;
- provide the LVR to the reviewing actuary for the purpose of peer review; and
- provide the FCR and the LVR to APRA on or before the day that the insurer's yearly statutory accounts are required to be given to APRA in accordance with reporting standards made under the *Collection of Data Act*.

QBE's board, and we assume the boards of most other insurers, will want to review all these documents prior to approving the annual financial report. The time frame for this is extremely tight to meet ASX's requirement to lodge results within two months of the year end. QBE believes that this will require significant additional resources and increase our cost of compliance due to the use of both further internal and external resources.

QBE is strongly of the opinion that the FCR has only limited value, as it merely duplicates other reports already prepared for QBE's board.

3.3 Responsibility for the FCR

Within paragraphs 43 to 45 of GPS 310, APRA proposes that the approved actuary be solely responsible for the production of a FCR. APRA is of the firm belief that only the approved actuary is objective enough to complete the FCR, although APRA recognises (in its discussion paper) that not all actuaries will "initially have the necessary skills".

QBE has previously suggested an alternative to APRA, which is that the FCR should be completed and signed by the senior management team, including the approved actuary. QBE strongly believes that the FCR should have sign off from both the CEO and CFO due to their intimate knowledge of the business. This suggestion has been rejected by APRA.

QBE still believes that many general insurance actuaries do not have the necessary skills and experience to take full responsibility for completing a meaningful FCR. The approved actuary would be required to place heavy reliance on senior management in drawing conclusions on items outside his or her own areas of expertise, in our view reducing the value of the document. It will also increase the costs of compliance as approved actuaries are required to spend additional time understanding those items in the report that are currently outside their areas of expertise.

We recommend that APRA reconsider the content and responsibility for the FCR to allow for more input by senior and executive management, in order to achieve an accurate, balanced and meaningful document that can be relied upon both by the insurer and APRA.

3.4 Scope of the audit report

GPS 310 at paragraph 42 states that the approved auditor's report must specify the results of investigations on whether:

- the insurer has systems, procedures and controls in place which are effective in ensuring compliance with all prudential requirements (including requirements imposed by the Act, the regulations, prudential standards, the Collection of Data Act and any other requirements imposed by APRA in writing) or if not, provide details of reasons supporting such an opinion; and
- the insurer has systems, procedures and controls in place which are effective in ensuring that reliable statistical and financial data is provided to APRA in the quarterly returns or if not, provide details of reasons supporting such an opinion.

QBE believes that the audit reports which are currently produced in relation to its business provide a significant level of detail to satisfy APRA both from a prudential and process perspective, as to whether there are any issues which require attention. The further requirements in GPS 310 unnecessarily broaden the scope of work undertaken by the approved auditor and hence will merely increase compliance costs for insurers with little or no benefit to Australian policyholders.

3.5 Continuous compliance with minimum capital requirements (MCR)

GGN 310.1 at paragraph 22 requires that the approved actuary comment on whether the insurer is complying with the MCR and has complied with the MCR continuously over the past year.

QBE objects to this proposal, as the approved actuary may not have access to systems or data confirming continuous MCR compliance.

QBE believes that the role of the approved actuary is to focus on the insurance liabilities in preparing their report, rather than assessing the insurer's compliance with the MCR. As an alternative, we believe that the approved actuary would be able to merely state that the company has complied with the MCR at each quarter end and that he or she is not aware of any breach of compliance with the MCR.

It should also be noted that most insurers would not have the capacity to calculate the MCR on a daily basis due to system constraints, timing issues and resource allocation. That said, we believe APRA can take comfort that breaches by QBE would be minimal if any, as a result of us being aware of any large claims, catastrophes (and their potential impact) through our internal reporting processes.

On that basis, we believe the requirements under GGN 310.1 at paragraph 22 are unnecessary and merely impose further time and costs on the part of the approved actuary.

ISSUE 4. GOVERNANCE AND INDEPENDENCE

The insurance industry is an important sector of the wider financial community in Australia. It plays a major role in facilitating a stable operating economy in all areas such as legal, banking and the financial markets.

As a major Australian insurer, QBE has raised the issue of governance and in particular, independence, with APRA on previous occasions, including the inconsistency that exists between APRA's proposed reforms (GPS 510 at paragraph 23 and GPS 511 at paragraph 20), and the Corporations Act and recommendations of the ASX Corporate Governance Council.

APRA's draft proposals seek to impose a restriction on executives of a company becoming the chair of an insurer or NOHC within three years of being employed in an executive position. Unfortunately, these proposals adopt a narrow focus entirely on independence without giving any credence to corporate memory or experience. Under current regulatory requirements in the UK, the CEO could become the chair. Australia needs to remain consistent with current international practices.

The success of a general insurance business, both from a prudential and profit perspective, relies on a unique skill set from its executives and directors to deal with the risks involved in the industry. These risks are quite distinct to other industries within the financial sector such as life insurance or banking. Insurance executives and directors require both specialist training and meaningful industry experience in order to provide strong leadership and governance in the current business and regulatory environment.

QBE believes that insurance boards need successful insurance executives with such in-depth knowledge and expertise, in particular relating to directing and managing an insurance company. As such, the pool of available directors within Australia with such experience is limited and with the proposals from APRA in their current form, the pool will become further limited.

QBE also believes this proposal focuses too much on the chair. In contrast to the US, it is not common in Australia to have an executive chair. A chair in Australia usually does not have a casting vote. A more important safeguard is a majority of independent, non-executive directors.

QBE recommends that these requirements be removed from the draft prudential standards. Should APRA continue to insist on restricting the ability of executives becoming the chair, QBE believes the draft standards should at least be made more flexible by providing APRA the discretion to consider and respond to a proposal submitted by the board of an insurer or NOHC requesting to have such an individual as its chair.

ISSUE 5. INCONSISTENCY OF GENERAL INSURANCE REGULATION FOR DIRECT OFFSHORE FOREIGN INSURERS

QBE believes there is a glaring inconsistency in the regulatory treatment of Direct Offshore Foreign Insurers (DOFIs) to local Australian regulated insurers, in relation to prudential supervision and the collection of various taxes.

With the increase in the prescriptive (rather than principles based) regulation and the general "regulatory overload', placed on Australian regulated insurers, QBE and other Australian regulated insurers are placed at a competitive disadvantage to DOFIs, who are able to insure Australian risks without being required to meet any level of regulation. This has the affect of making insurance companies more compliance focussed and therefore risk averse, and at the same time significantly increasing costs and encouraging the proliferation of non regulated products due to the expansion of DOFIs in the Australian market place, for which we have noticed a significant increase during the past 2 years.

That said, QBE agrees with the option of providing an exemption from prudential regulation for DOFIs marketing insurance in Australia which are domiciled in a country APRA considers to have comparable prudential regulation, such as QBE's subsidiary in London.

However, this is on the basis that those DOFIs writing Australian risks will not only be subject to comparable prudential regulation, including reporting requirements, but also to equivalent taxes on the business written in Australia. Policyholders must pay the total amount, including relevant taxes and not have the competitive advantage of avoiding payment of such taxes.

QBE is not seeking new regulation in this respect. Rather, we seek equal treatment for local insurers and DOFIs wishing to write Australian risks.

In particular, QBE is concerned about the significant tax advantages enjoyed by DOFIs. As a major Australian insurer and top 20 Australian listed company, QBE is keen to have fair price and other competition, and ensure all insurance policies covering Australian risks, whether insured by an Australian insurer or a DOFI, are subject to the same level of tax enforcement.

While a number of state and federal taxes are imposed on Australian insurance business written offshore by DOFIs, we understand that when compared to business written by Australian resident insurers, there is a disparity in relation to the collection (as opposed to the imposition) of such taxes, both from the DOFI and the insured. These taxes include federal income tax, state stamp duty, fire services levy, GST, withholding tax and the NSW Insurance Protection Tax.

As these tax regimes are strictly enforced on Australian resident insurers, we suggest that DOFIs be required to pay the same taxes as resident insurers, and that a monitoring and audit regime be introduced to ensure that these taxes are collected.

QBE also notes that it is more than 18 months since the Potts recommendations were published, Treasury is yet to provide any draft regulation and/or other legislation to demonstrate how these important issues will be addressed.

ISSUE 6. DEALING WITH REGULATORS

6.1 Working relationship with regulators

QBE strives to maintain a good working relationship with all regulators with whom it deals. On that basis, we believe QBE's experiences have so far been positive and dealt with in a spirit of cooperation. However, that is not to say improvement is not required.

As our prudential regulator, QBE's most frequent contact is with APRA. This relationship is on two levels, one being through consultation relating to the formation of regulation and the other through our ongoing relationship on day to day prudential matters. In QBE's view, APRA is generally consultative, but determined in their approach depending on the issue being discussed. Through QBE's allocated liaison officer at APRA, our contact with APRA tends to be regular and on a personal level.

Our dealings with ASIC, on the other hand, have tended to be on a more formal basis conducted through written correspondence. We believe there is a reluctance on the part of ASIC to meet with their clients and discuss issues. If ASIC was prepared to allocate a liaison officer for QBE and adopt a more relaxed approach through personal meetings, we believe a more effective working relationship could be achieved, leading to better communication and understanding of each parties needs and earlier resolution of issues.

Three areas in which improvements could be achieved are:

6.2 Communication from ASIC to QBE

There have been instances, primarily with ASIC, where QBE has complied with a Notice to produce documents or provide information, and has either not received a reply to advise that ASIC has no further issue, or a reply has only been forthcoming after a considerable amount of time has passed.

QBE believes in due course, ASIC (and other regulators) should always provide a response clarifying that it has no further issue/s to be addressed, so that QBE is advised that no further action is required and is able to finalise the matter.

6.3 Meeting with ASIC

In the instances where ASIC requires documents or information from QBE, much time and cost could be saved for both parties, if ASIC were prepared to meet with QBE prior to issuing their Notice and discuss their requirements. At that meeting, both parties would gain a clearer understanding of the other's needs and be able to focus resources more efficiently. For example, the broadly drafted Notices issued by ASIC in their recent enquiry undertaken into Brokers Commissions involved many hours of locating documents and much correspondence with ASIC to try and establish exactly what material they were seeking.

6.4 Communication between regulators

QBE believes that while all regulators are seeking to achieve a stable and robust financial services industry in Australia which facilitates fair competition by all market participants, a fundamental barrier to achieving this goal exists, due to the current lack of communication and cooperation between regulators.

This lack of communication manifests itself primarily through overlaps and inconsistency between the regulators' requirements, examples of which have been provided above.

Once an overlap or inconsistency does occur, there needs to be efficient and effective liaison between the relevant regulators to address this issue. The responsibility for addressing overlaps and inconsistencies should rest with the regulators.