INSURANCE COUNCIL OF AUSTRALIA

Submission to the Australian Government Regulation Taskforce

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Contents

1 Executive summary

In recent years, the regulatory burden on general insurers has increased sharply.

The Wallis Inquiry resulted in sweeping reforms across the sector, including a fundamental overhaul of the *Insurance Act 1973* (Insurance Act). Financial Services Reform (FSR) required insurers to obtain new licences and to rewrite documents to comply with a cross industry disclosure regime. Reforms that spread across various sectors of the economy such as GST and private sector privacy regulation required significant change within the financial sector. Recently, a second generation of reforms was initiated, with proposed amendment to prudential standards under the Insurance Act and refinements to FSR.

Many of these reforms instituted positive change in the industry. Change to prudential regulation saw the introduction of risk-based regulation. Licensing of financial service providers improved training standards and service quality for consumers. Privacy laws formalised a long tradition of insurers handling customers' confidential information with care.

However, the volume of new regulation combined with a prescriptive "one size fits all" regulatory design has resulted in high compliance costs. Larger insurers (over 500 employees) have indicated ongoing compliance costs range from $18-20 million per annum. Both large and small insurers have indicated that compliance issues now consume between 10% and 25% of senior management and Board time.

The present, marking a decade since the Wallis Inquiry, presents a timely opportunity to take stock of the regulatory burden. ICA welcomes the Regulation Taskforce and applauds the steps taken by the Prime Minister and Treasurer to address unnecessary regulatory burden.

In this submission, ICA makes the following key recommendations for alleviating the burden of regulation:

- Increase the use and accuracy of cost benefit analyses together with the depth and frequency of consultation prior to new regulation being introduced;
- Establish a Bureau of Financial Sector Regulation to improve the accountability and monitoring of financial sector regulators;
- Implement the package of reforms recommended by the HIH Royal Commission that were intended to improve the regulatory environment and which were accepted by the Government but remain outstanding, namely the regulation of all insurance and insurance-like products, removal of overlaps between State and Federal prudential regulation, a light touch safety net for policyholders and removal of a number of excessive State taxes on insurance; and
- Reduce overlapping and otherwise excessive regulation in other areas, most urgently by tailoring the dollar disclosure provisions of FSR to general insurance.

ICA makes a total of 27 recommendations which are set out in Appendix 1. ICA strongly urges the Regulation Taskforce to consider immediate concerns of business that can be addressed relatively quickly to relieve red tape, together with longer term systemic problems – such as the limited use of consultation, cost-benefit analyses and post implementation reviews – that will contribute to high costs of regulation in future.

2 Introduction

The Insurance Council of Australia (ICA) is the representative body of the general insurance industry in Australia.

ICA membership represents more than 90 percent of total premium income written by APRA authorised private sector general insurers.

ICA members provide non life insurance products ranging from those usually purchased by individuals (such as home and contents insurance, travel insurance, motor vehicle insurance) to those purchased by small businesses and larger organisations (such as product and public liability insurance, workers compensation, commercial property, and directors and officers insurance).

ICA members, both insurers and reinsurers, are regulated and licensed by the Australian Prudential Regulation Authority (APRA) and are a significant part of the financial services system. Recently published statistics from APRA show that the private sector insurance industry generates direct premium revenue of $28.4 billion per annum and has assets of $80.1 billion.[1] The industry employs about 43,000 people.[2]

Australian general insurers issue more than 41 million insurance policies annually and deal with 3.5 million claims each year.[3] The industry provides protection for a substantial amount of Australia's assets, held by households, governments and businesses. On average, about $55 million in claims is paid each working day.

Insurance allows individuals to engage in risky activities, such as starting up a business because it an insurer is better able to absorb losses. Insurance plays an important role in ensuring the smooth operation of the national economy. The collection of premiums by insurance companies also provides a mechanism by which savings are mobilised.[4]

Having regard to the importance of insurance for individuals and the economy as a whole, it is essential that regulation of insurance achieve the proper balance between protecting policyholders, consumers, and efficiency. This submission seeks to assist in achieving that balance and is made to the Regulation Taskforce announced jointly by the Prime Minister and Treasurer on 12 October 2005 (Taskforce).

3 Burden of regulation on general insurers

The exact impact of regulation[5] on insurers is difficult to quantify. However, some key indicators of the direct cost of regulation and the opportunity cost of the resources consumed by compliance follow.

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[1] APRA, *Quarterly General Insurance Performance, June 2005.*

[2] ICA Human Resources Standing Committee Research October 2005

[3] APRA *Selected Statistics on the General Insurance Industry, Year Ending June 2002*

[4] Centre for International Economics "The General Insurance Sector: Big Benefits but Overburdened" (August 2005) prepared for the Insurance Council of Australia page v

[5] This submission adopts the defining of "regulation" set out in the Regulation Taskforce Issues Paper p2: "to include any laws or other government 'rules' which influence or control the way people and businesses behave. Under this definition, regulation is not limited to legislation and formal regulations; it also includes 'quasi-regulation' (such as codes of conduct, advisory instruments or notes etc)".

Our members have indicated that there has been a dramatic increase in overall compliance costs over the past 5 to 10 years. For larger insurers (over 500 employees), ongoing compliance costs range from $18 - 20 million per annum. Two medium size insurers have estimated that their total compliance costs amount to $5.5 million and $7.4 million per annum respectively. Smaller insurers (under 500 employees) report compliance costs in the order of $5 million per year.

Both large and small insurers have indicated that compliance issues now consume between 10% and 25% of senior management and Board time. The need to focus on compliance at the senior management and Board level also runs the risk of stifling innovation and creativity. One small insurer has estimated total senior management time spent on compliance is five times greater than five years ago and ten times greater than ten years ago.[6]

Compliance with regulation has a disproportionately high impact on small insurers with fewer than 500 employees. For example, one small insurer has indicated that compliance expenses as a percentage of operating income has risen from a base of 0.8% ten years ago, to 0.9% five years ago to 2.1% in 2005.

These costs of compliance are inevitably reflected in the premiums, distorting the prices that consumers must pay.

The key factors that contribute to high costs of compliance are:

- The level of complexity in insurance regulation;
- The rapid change in insurance regulation; and
- The volume of regulation.

Each of these factors is discussed below.

3.1 Complexity in insurance regulation

General insurers are subject to a complex regulatory environment. Regulation in this sector is characterised by overlapping responsibilities of regulators, inconsistent and sometimes unnecessary regulation. There is also a significant gap in regulation, which means that high costs are imposed on some insurers, while relatively low regulatory requirements are imposed on others. These are set out in the map in Appendix 2.

Industry specific regulation at the Federal level includes the Insurance Act for prudential supervision, the *Insurance Contracts Act 1984* (IC Act) for consumer protection and Institute of Actuaries of Australia as well as APRA accounting standards. State and Territory Governments also subject insurers to prudential supervision, deal with aspects of market conduct and consumer protection and the various statutory insurance schemes, which operate in each State and Territory.

In addition to industry specific regulation, general insurers are also subject to the regulation that applies across the financial sector, most notably FSR. The industry is subject to the corporate regulatory regime that applies to Australian incorporated businesses generally. This includes the

[6] That small insurer indicated that where compliance matters took 104 hours of senior management time ten years ago, that figure rose to 195 hours of senior management time five years ago and has since risen to 1014 hours per month in 2005.

legislative regimes of the *Corporations Act 2001* (Corporations Act), the *Trade Practices Act 1974* (TPA) and for public listed companies, the requirements of the Listing Rules of the Australian Stock Exchange (ASX).

Regulation that applies to multiple sectors is also complex. This is felt acutely in the area of taxation and accounting, where insurers are required to keep three parallel "books" in order to comply with their taxation obligations, insurance accounting and APRA reporting requirements.

3.2 Rapid change in insurance regulation

Over the past decade, this complex regulatory environment has undergone dramatic change.

The Wallis Inquiry of 1996 resulted in sweeping reforms across the sector. Following the collapse of the HIH group of companies in 2001, the Insurance Act underwent a major overhaul and a number of new prudential standards were introduced. It improved regulation of general insurance by introducing a risk based capital requirement, incorporating a requirement for significant prudential margins to be held by insurance companies.

In 2002 the new licensing and disclosure regime for financial services in the form of FSR required insurers to obtain new licences and to rewrite documents. Over the same time-period, reforms that spread across various sectors of the economy, including the introduction of GST and application of the Privacy Act to the private sector, also required significant change within the financial sector.

In 2003, a second generation of reforms were initiated by APRA to amend prudential standards and earlier this year a package of refinements to FSR was proposed. Together with these changes, other changes to the Corporations Act, TPA and Insurance Act, are proposed. A list of proposed changes to regulation which have a direct and significant impact on the insurance industry is set out in Appendix 3.

3.3 Volume of insurance regulation

The volume of regulation in general insurance is best measured by the structures and procedures that insurers put in place in order to comply with that regulation. These include:

- A suite of committees

Typically an insurer will have at least one of each of the following committees staffed by senior management and middle management: risk management committee, risk management subcommittees, audit committee, compliance committee and dispute resolution committee. This suite of committees assists insurers to maintain a robust compliance framework.

- Growing compliance groups

A large insurer has indicated that staff numbers in compliance groups have grown by 20-30% in the last two years alone. A medium sized insurer has reported that ten years ago they had one lawyer doing all compliance work, plus additional time from accounting and internal audit staff; five years ago this had increased to two in house counsel, with increased contributions required from accounting, internal and external audit staff; and currently it employs a full time compliance manager, four in house counsel, an actuary plus external assistance, enlarged accounting, internal and external staff, plus substantial compliance costs throughout the organisation.

Compliance groups are required to perform new tasks required to meet with regulation, including:

- Development and implementation of training resources and materials – including on line training modules and purchase of software licences;
- Conducting training sessions for staff;
- Developing incident reporting tools and the monitoring, reporting and rectification of incidents;
- Preparing manuals particularly for authorised representatives;
- Appointing and monitoring authorised representatives;
- Spending many minutes per phone call reading prescribed scripts;
- Monitoring and complying with obligations to report material FSR breaches to ASIC and all breaches to APRA; and

- Higher demand for auditing and actuarial resources

Increased audit reporting has raised costs of retaining auditors together with developing processes to support audits, staff and management time. These costs have increased significantly in the past three years since the introduction of the new APRA regime which requires additional audit of APRA returns and imposition of the annual targeted review process.

- Staff time spent on compliance

Sales staff, including call centre staff, spending many minutes per phone call reading prescribed scripts. Typically, this would include:

- General Advice Warning that complies with FSR;
- Duty of Disclosure Statement that complies with the *Insurance Contracts Act 1984*; and
- Privacy Statement that complies with the *Privacy Act 1988*.

ICA has estimated that the ongoing cost of giving privacy notices over telephone sales costs the industry between $1-2 million per annum due to the ongoing costs of training, staff time and other compliance considerations.[7]

- Growth in tax compliance

The continuous additions to the income tax legislation have contributed to the need for large tax groups within large insurers and a heavy reliance on external expert taxation advice for small insurers. The introduction of the GST led to a rapid increase in the volume of taxation regulation with which insurers must comply. Initial costs included systems changes, staff training and expertise development. Having now been in place for some years, it is clear that the GST has transformed tax compliance from a simple function that could largely be performed by automated systems into a complex area of regulation. Where, for example, claims clerks could once process claims simply,

[7] ICA submission on Issues Paper – Review of the Privacy Act – Private Sector Provisions (December 2004) p18

senior claims clerks and taxation experts are now called upon to intervene and assess the way in which the tax law applies to a claim.

- Increasing consumption of legal resources

Legal resources have become necessary to assist with compliance in the following areas:

- Preparing documentation specific to regulatory requirements such as the Corporations Act and IC Act;
- Ensuring that marketing materials comply with relevant regulatory requirements; and
- Preparing scripts for telephone sales and inquiries.

Having regard to these costs of compliance, together with the pace of change, the complexity of the regulatory environment and the volume of regulation, ICA makes 27 recommendations for improving insurance regulation in the following section.

4 Improving insurance regulation

Improving insurance regulation requires reform in three key areas: firstly, the process of implementing regulation undertaken by the regulators; secondly, high-level reform of insurance regulation recommended by the HIH Royal Commission; and thirdly, a reduction in unnecessary regulatory burden in other areas of overlapping, inconsistent, complex or excessive regulation.

4.1 Improving regulatory process

The processes of regulation in the financial sector, including the design, implementation and supervision of regulators, has recently been the subject of a Report produced by CRA International for the Finance Industry Council of Australia (FICA) (Report).[8] ICA is a member of FICA and endorses each of the recommendations of that Report, a copy of which forms Annexure A to this submission.

The Report makes a total of eleven recommendations. Based on the premise that "prevention is better than cure", the recommendations are made to encourage the design of less prescriptive regulation, ensure an outcome-oriented culture within financial sector regulators, develop a stronger information base, boost the monitoring and accountability of regulators and advocate flexible approaches to regulation in international fora. ICA supports each of the Report's recommendations as set out below.

[8] CRA International for the Finance Industry Council of Australia (FICA) (7 November 2005)

Recommendation 1

Following the policy framework articulated in the Wallis Inquiry, the Government should be encouraged to adopt light-handed models of regulation in the major reviews of regulations currently under way. The implementation of these regulations, as for all regulation, should use the minimum level of market intrusion necessary to give effect to the identified policy objectives. It should be proportionate to the demonstrated market failure and applied efficiently.

Recommendation 2

Consultation should be comprehensive focused on ensuring the most cost-effective means to achieve the stated policy intent of any new or substantially modified financial sector regulations be undertaken at all stages of the development of the regulations i.e. when policy is designed, legislation is drafted, and the legislation is translated into specific regulations and procedures applied by the relevant regulator.

Recommendation 3

The business community should continue to support a broad debate on the need for further microeconomic reform, with the development of well-designed regulations being an essential element of that agenda.

Recommendation 4

For major pieces of financial sector regulation, the Government should release a statement of policy intent, initially in the form of its 2nd reading speech and thereafter conduct a post implementation review within two years to measure whether the objectives were being achieved in the most cost effective manner.

Oversight and co-ordination of regulators

ICA supports the current Commonwealth regulatory framework covering the financial services sector with:

(a) APRA responsible for prudential regulation,

(b) ASIC responsible for market conduct regulation,

(c) ACCC responsible more broadly for competition matters and consumer protection, and

(d) ATO responsible for the implementation of Commonwealth taxation laws.

However, as the Report concludes, there is a strong argument for improvement in the oversight and co-ordination of Regulators.

The Report calls for a new body *to monitor and assess the appropriateness of how regulations are being implemented in detail.*

ICA recommends that a Bureau of Financial Sector Regulation (Bureau) should be established to improve the accountability of and monitoring of regulators and to oversee the implementation of the Government's regulatory policy for the financial services sector. Responsibility for much of the oversight of financial sector regulation be devolved to the Bureau. In brief, the Bureau would have three main functions:

- The identification and filtering of issues;
- The development of a deeper understanding of the costs and benefits of financial sector regulations; and
- As a public voice for best-practice regulation in the financial sector.[9]

The Bureau would not function as a "super-regulator". Rather, like the Inspector-General of Tax, it would be tasked explicitly with reviewing only systemic issues that may lead to recommendations involving policy design and regulatory practice.

Part of the role of the Bureau would be to have regard to the co-ordination of ASIC and APRA's roles. Formal measures require APRA and ASIC to facilitate co-ordination are currently in place:

"*The agencies agree that consistent with their separate roles they will co-operate where it is within their administrative powers to reduce duplication and compliance costs and achieve effective enforcement and compliance outcomes.*"[10]

However, there is ample evidence that these formal measures are not being fully applied. For example, over mid 2005, both APRA and ASIC were consulting insurers on major reforms. This limited the ability of insurers to engage thoroughly in each of these consultations. There is a clear role for the Bureau in overseeing and co-ordinating regulators, including the timing of consultation.

Recommendation 5

A Bureau of Financial Sector Regulation should be established to oversee financial sector regulation.

Cost-benefit analyses

The Report reviews the path of regulation set down by the Wallis Inquiry.[11] Wallis advocated "light-handed" regulation in financial services which relies on market discipline where possible, is based on principles rather than prescribing processes and encourages alternatives to regulation.

However, the idea of light handed regulation was overtaken by events.

Much recent regulation has suffered from a lack of thorough cost-benefit analysis and robust consumer testing. Although the Office of Regulatory Review has an extensive role "on paper" it has had relatively little influence in practice.[12]

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[9] CRA International for the Finance Industry Council of Australia (FICA) (7 November 2005) at 36

[10] Memorandum of Understanding 1.2

[11] Financial System Inquiry *Final Report* 1997 at www.fsi.treasury.gov.au

[12] CRA International for the Finance Industry Council of Australia (FICA) (7 November 2005) at 37

In particular, the FSR has been criticised for the lack of analysis of the benefits that consumers gain from the complex and cumbersome disclosure regime, relative to the costs of complying with that regime. Following the implementation of FSR, industry has been left to address systemic issues with the FSR regime by making applications to ASIC for class orders, each of which have may only address a limited part of a much broader area of concern. A good example of this has been the dollar disclosure provisions (and ensuing class orders) which is discussed in detail in paragraph 3.3.1 of this submission.

Together with consumer testing where legislation is intended to provide consumers with protection or benefits, cost benefit analyses are fundamental to the health of the regulatory system. They go hand in hand with a sustained and thorough consultation period. They should not be restricted to legislation but should be undertaken, where appropriate, for regulations and disallowable instruments such as APRA prudential standards.

Accordingly, there is a role for the Bureau in contributing to accurate cost assessments by developing a deeper understanding of the costs and benefits of financial sector regulation and lifting the standards of cost-benefit analysis.

Recommendation 6

The Bureau of Financial Sector Regulation should be tasked with the development of common methodologies to calculate the costs of complying with financial sector regulation. The Bureau should work closely with FICA (or the different industry associations) to help to ensure that this effort is as cost-effective as possible.

Recommendation 7

The Bureau of Financial Sector Regulation should be given a mandate to lift the quality of the cost-benefit analysis of financial sector regulation, and be resourced adequately for this task. The Bureau should encourage a deeper understanding of best practice regulation.

Recommendation 8

The Government should recognise the potential usefulness of regulated entities being able to develop their own compliance models to achieve regulator-specified outcomes. APRA and ASIC, in particular, should be encouraged to define what is expected of regulated entities and to develop a framework for alternative compliance models for specified areas of regulation.

Recommendation 9

The Reserve Bank should be encouraged to reconsider its current approach to the regulation of interchange and explore less constraining means to encourage appropriate competition.

Recommendation 10

The Bureau of Financial Regulation should have a mandate to monitor areas of duplication and inconsistency across regulators.

Recommendation 11

The Government should continue taking a lead in the developing of outcomes-based models of regulation in international forums. It should also encourage the recognition that regulatory frameworks may need to evolve as specific regulations are made operational. In adoption of international standards, Australian legislators and regulators should take due regard to the impact of early adoption on international competitiveness of domestic players.

4.2 Improving the regulatory environment

In its submissions to the HIH Royal Commission, ICA identified a range of weaknesses in the regulatory environment that partially contribute to the conditions in the HIH Group of companies collapsed.

ICA developed and submitted a blueprint for insurance regulation to the HIH Royal Commission. Many components of the blueprint for insurance regulation were accepted by the HIH Royal Commission in its recommendations to the Government, including a package of inter-related reforms, being the four components of the blueprint.

ICA's blueprint for insurance regulation is designed to strengthen and simplify the regulatory framework. The foundation of that blueprint is that all insurance and insurance-like business is regulated. That means that the gap that currently allows Discretionary Mutual Funds (DMFs) and Direct Offshore Foreign Insurers (DOFIs) to avoid prudential regulation is removed. Once the base of regulation is properly established, then it is necessary to overcome the duplications and inconsistencies created by State/Federal overlap, State/State inconsistency, to introduce a policyholder protection scheme and to remove the taxes that affordability of general insurance.

Making this package of reforms a priority should improve the efficiency of the sector.

4.2.1 Regulation of all insurance business

Not all insurance or insurance-like business is subject to the same prudential regulation.

Under the Insurance Act, an insurer that carries on insurance business in Australia must be authorised by APRA. The main object of the Act is the protection of the interests of policyholders and prospective policyholders under insurance policies in ways that are consistent with the continued development of a viable, competitive and innovative insurance industry.[13]

Under that Act 'insurance business' is defined in 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... .'[14]

There are restrictions to the scope of the Insurance Act that arise in the context of the definition of 'insurance business'. The threshold requirement is an undertaking of liability. Discretionary entities and insurance mutuals, whilst they offer protection in the nature of insurance, do not undertake

[13] Section 2A of the *Insurance Act*.

[14] Section 3 of the *Insurance Act*.

liability and are not captured. [15] DOFIs that do not have a branch in Australia or who do not actively solicit business in Australia are not prudentially regulated.

- Consumer protection

More Australian policyholders would be protected, and the strength and viability of the general insurance market in Australia could be enhanced if all entities underwriting general insurance or offering insurance like arrangements were regulated by the Insurance Act.

A range of entities currently undertake the business of general insurance or arrangements of the nature of insurance outside the requirements of the Insurance Act. These entities include mutual organisations and government insurers.

As a result, the interests of significant numbers of policyholders or people with indemnity arrangements are not protected under the Insurance Act.

If the requirements of the Insurance Act applied to such entities, more policyholders could enjoy the security afforded by the prudential standards under the Insurance Act, and the benefits of the policyholder protection scheme proposed below by ICA.

- Competitive neutrality

At the heart of the argument for competitive neutrality is the fact that consumers have choices when it comes to their insurance decisions and for the most part that choice is made based on price. The regulatory burden is a factor affecting insurers costs, but the biggest issue around competitive neutrality is taxation. The tax advantage granted to these unauthorised players is significant and it is real.

While technically insurance policies offered by DOFIs are subject to these taxes as they are payable by the policyholder if the insurer is not registered, there are little if any enforcement mechanisms to ensure that these taxes are paid. Since the products of DMFs are not considered to be insurance, they are able to avoid these punitive taxes completely. The Potts Review found that DMFs benefit from significant cost advantages over authorised insurers, because their exemption from State taxes and prudential regulation and that DOFIs enjoy significant tax advantages over Australian authorised insurers.

A uniform and consistent framework for the prudential regulation of all entities underwriting insurance or offering insurance like arrangements would enhance a fair, open and competitive market for general insurance in Australia, and potentially increase the size and strength of the insurance market.

These outcomes can be best achieved by:

(a) The Commonwealth exercising, to its fullest extent, its constitutional power to make laws in respect of insurance;[16] and

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[15] In addition, there are a number of specific exclusions from the definition of 'insurance business' in section 3 of the *Insurance Act*. These exclusions relate to particular types of business that would otherwise be 'insurance business', such as life insurance which is governed by the *Life Insurance Act 1995 (Cth)*.

[16] The Commonwealth Parliament has constitutional power to make laws with respect to insurance, other than State insurance, but including State insurance extending beyond the limits of the State concerned. The Commonwealth has a very broad power to make laws with respect to insurance, except where such insurance can be categorised as State insurance not extending beyond the limits of

(b) To the extent that the Commonwealth's constitutional power is not sufficient to extend the operation of the *Insurance Act* to all entities underwriting insurance and arrangements of the nature of insurance, the establishment of arrangements between the States and the Commonwealth to ensure the consistent regulation of all entities underwriting general insurance or offering insurance like arrangements.

Preliminary developments

This issue was the subject of the 2003-2004 Review by Mr Gary Potts. The Potts Review made recommendations that DMF cover be offer as a contract of insurance under the Insurance Act but that DOFIs marketing insurance in Australia be exempt from prudential regulation in Australia if they are domiciled in a country Australia considers to have comparable regulation.

While the Potts recommendations go some way to addressing the issues around DMFs and DOFIs, they would not sufficiently address the problems of distorted competition and consumer protection.[17]

From a consumer protection perspective, ICA remains concerned that the primary source of protection for consumers, specifically having assets within the reach of the Australian regulator in the event of a corporate failure of an insurer, is not fully addressed in the Potts recommendations. For DOFIs, it is highly unlikely that a requirement to have adequate assets in Australia will be part of a comparable regulatory regime assessment. Consumers of DMFs that Potts recommends be exempt from APRA authorisation would not have the benefits of effective prudential oversight nor will they have any priority access to assets in the event of a failure.

Implementation of the Potts recommendations not only permits but encourages the presence of unauthorised insurers through setting out the rules under which these insurers can operate in Australia.

The only real solution for all stakeholders is to ensure that all insurance or insurance type business is effectively regulated. The prudential oversight provided through APRA regulation, combined with requirements to hold sufficient assets within reach of the jurisdiction in Australia, are critical consumer protections that benefit not only policyholders but the industry as a whole.

ICA understands that a response to the Potts recommendations is immanent and looks forward to working with the Government on creating an even playing field for Australian insurers.

Recommendation 12

The concept of 'carrying on insurance business in Australia', as set out in the Insurance Act, should be interpreted and applied so that all DMFs and DOFI providing protection for risks in the Australian market are regulated by APRA.

the State. That is insurance which is not 'State Insurance' and State insurance extending beyond the limits of the State is within the legislative power of the Commonwealth.

[17] For further detail, refer to ICA submission in reply to the Potts Recommendations

4.2.2 Removing overlap, duplication and inconsistency in prudential regulation

Overlap, duplication and inconsistency characterise the regulatory environment that insurers now operate in.

General insurers in Australia are potentially subject to differing regulatory requirements in eight jurisdictions for statutory insurance in relation to any of the following features of a particular scheme[18]:

- The prudential and financial regulation of general insurers involved in the scheme, either as underwriters of, or agents for the scheme;
- The setting of premiums for a scheme or supervision of price;
- Compensation or benefits and controls on access to certain types or levels of compensation or benefits;
- The regulation of service providers for a scheme such as the medical, health and legal professions;
- Claims handling and dispute resolution processes; and
- Mechanisms to deal with non-insured parties.

Duplication and inconsistencies between pieces of regulation arise largely because of two regulatory cleavages: first, overlapping regulatory responsibilities between APRA and State prudential regulators and secondly between State regulators.

State/Federal overlaps and inconsistencies

Currently each State/Territory licenses and conducts prudential oversight of any insurers that underwrite statutory classes of insurance (specifically Compulsory Third Party (CTP) and workers compensation) within its boundaries. For private insurers, this is in addition to APRA's prudential regulation that looks at all of an insurers book of business.

The justification that the States and Territories give for prudential oversight is that in the event of a failure of an insurer that underwrote either CTP or workers compensation within their jurisdiction the State/Territory would have to cover any liabilities as nominal insurer. This was the situation in NSW and Queensland as it related to the CTP business of the HIH Insurance Group and H.O.W.

ICA supports the recommendations of the HIH Royal Commission that the States and Territories not undertake any prudential regulation of general insurance, that APRA should be the sole prudential regulator[19] and that the States and Territories implement a process designed to reduce inconsistencies in their statutory schemes.

Recommendation 13

That the States and Territories not undertake any prudential regulation of general insurance.

[18] Appendix A lists general insurers and the statutory schemes for which they are either underwriters or agents in personal injury motor accidents, workers compensation and builders warranty insurance.

Inconsistent State/State Regulation

States and Territories responded in various ways to the need to provide guaranteed access to compensation or benefits for people suffering loss in certain circumstances such as employees injured at work or people injured in a motor vehicle accident. Appendix 4 provides an overview of statutory classes across the country.

Workers compensation provides a clear example of the problems of inconsistent regulation. The compulsory nature of workers compensation and its role in the broader industrial relations environment have resulted in a far more intense level of regulation and government intervention than any other insurance product. To date this regulation and government intervention has been almost entirely state-based in Australia (other than for Commonwealth employees and seafarers). The result is the current patchwork of different schemes for each State and Territory, plus specific national schemes for federal government employees and seafarers as well as special schemes such as the coal miners' in New South Wales. Each has evolved largely in isolation with very limited coordination at the national level. While all these schemes are under almost continual review there has been no change to the fundamental structure since the 1980s. Provision of workers compensation continues to be dominated by the state public sectors and licensed private insurers remain excluded from direct underwriting in four of the five larger states.

The HIH Royal Commission also recommended that the "States and Territories implement a process designed to reduce inconsistencies in their statutory schemes."[20] ICA continues to strongly support this recommendation.

ICA supports nationally consistent frameworks in the key areas of statutory classes and such frameworks would remove unnecessary costs and compliance burdens.

Recommendation 14

That the States and Territories implement a process designed to reduce inconsistencies in their statutory schemes.

4.2.3 Policyholder safety net

The third component of the package of reforms recommended by the HIH Royal Commission was that, "the Commonwealth Government introduce a systematic scheme to support the policyholders of insurance companies in the event of the failure of such a company".[21]

The existence of such a scheme is the ultimate form of consumer protection and underpins foreign regulatory regimes such as those in the United Kingdom and Canada.

ICA supports the introduction of an appropriate policyholder protection scheme as part of the package of reforms discussed above.

[19] Recommendation 49

[20] Recommendation 51

[21] Recommendation 61

Prudential regulation of DMFs and DOFIs is the primary step. If a policyholder protection scheme was introduced without proper regulation of DMFs and DOFIs, a levy on Australian authorised insurers would encourage further growth in the use of unregulated insurers.

The creation of a PPS should be tied to States' and Territories' removing themselves from prudential regulation and shutting down their nominal defendant and nominal insurers schemes that activate when an insurer fails. If a policyholder protection scheme were introduced before the removal of States and Territories from prudential regulation, then there would be duplication in those schemes. A well-designed PPS that provides the same level of protection as the existing nominal insurer arrangements would nullify this threat to state finances. A State or Territory government would still have the right to impose licensing controls on insurers that operate within its borders, but would bear no financial risk for their operations. Thus, there would be no need for a nominal insurer type arrangement to exist in case of insurer failure and, similarly, no plausible justification for continued prudential oversight. The introduction of a PPS that has a benefits structure at least equivalent to the nominal insurer arrangements must result in the States and Territories ceasing to conduct prudential regulation.

The industry's preferred model for a policyholder protection scheme has been articulated in a number of submissions. Essential points are:

- Post event funding through a levy on all insurance products;
- Independent industry administration with participation a condition of APRA licensing;
- Eligibility for benefits limited to individuals who are Australian citizens or permanent residents; small businesses with turnover of up to $1 million and all policyholders under eligible statutory schemes; and
- Benefit levels of 100% for of the policy coverage personal injury motor accidents and workers compensation schemes, 100% up to $5,000 for all other claims and 90% of the policy coverage for the remainder of that amount up to a maximum of $500,000.

In mid November 2005 further support was lent to the policyholder protection scheme. The Council of Financial Regulators supported a model for a safety net for general and life insurance policyholders as well as deposit holders. Whilst ICA supports a scheme that is specific to general insurance, ICA welcomes such steps towards giving effect to the HIH Royal Commission package of reforms.

Recommendation 15

That the Government introduce a systematic scheme to support the policyholders of insurance companies in the event of the failure of such a company, as part of the package of reforms of insurance regulation.

4.2.4 Direct taxes on insurance

General insurance is one of the most highly taxed industries in Australia and Australian general insurers are some of the most highly taxed general insurers in the world. The Centre for International Economics' August 2005 Report concluded that: "[d]espite the unique importance of insurance in the

Australian economy, current tax arrangements place a punitive burden on the industry that is out of line with tax levels in other countries."[22] In 2003-2004 the States and Territories took in more than $2 billion in stamp duty on insurance and $550 million[23] in fire service levies for those states where this antiquated form of funding the fire brigades remains.

Taxes include the Australian Income Tax and Capital Goods Tax, Stamp Duty, Superannuation Surcharge/Guarantee, NSW Insurance Protection Tax, Fire Services Levy, Interest Withholding Tax, Payroll Tax, Land Tax, Goods & Services Tax, Fringe Benefits Tax and Pay As You Go Withholding.

Some State taxes, such as the Fire Services Levy, have different requirements in different jurisdictions, which adds to the regulatory burden involved in developing systems, accounting and specialist taxation staff. Some of these taxes are calculated in a cascading manner. GST is calculated in top of the FSL and stamp duty is applied on premium including both of these taxes.

The impact of insurance premium taxes on consumers was the subject of an independent study looking at the effect of removing the Emergency Services Levy in Western Australia on property insurance premiums. According to this report, the "removal of FSL in Western Australia contributed to Western Australia having one of the most price competitive insurance markets in Australia in 2003" with buildings and contents insurers dropping their premium rates.[24]

The HIH Royal Commission made a suite of recommendations for State tax reform in general insurance. It recommended that State and Territory governments abolish stamp duty on general insurance products, those States that have not already done so abolish fire services levies on insurers, State and Territory governments exclude the cost of the GST for the purposes of calculating stamp duties on any other state or territory levies that are imposed on insurance premiums and that governments avoid imposing on insurers levies and other taxes that cannot be passed on to policyholders (i.e., NSW Insurance Protection Tax).

These unequivocal recommendations were supported by arguments that high insurance taxes led to consumers making decisions to underinsure or not insure at all, or to consider unregulated alternatives.

Despite the urgings of ICA, the HIH Royal Commission and other business and industry groups such as the BCTR and ACCI, all of which support abolition of insurance taxes, limited action has been taken by governments.

Recommendation 16

That State and Territory governments abolish stamp duty on general insurance products.

Recommendation 17

That those States that have not already done so abolish fire services levies on insurers.

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[22] Centre for International Economics "The General Insurance Sector: Big Benefits but Overburdened" (August 2005) prepared for the Insurance Council of Australia page vi

[23] Source 2003-04 Budget Papers for the States and Territories.

[24] *Consumers have responded to cheaper insurance by increasing their insurance cover to more adequately protect themselves." Emergency Services Levy Insurance Compliance Review: Final Report*, Sigma Plus Consulting, April, 2004, p. 3. The report goes on to demonstrate that sums insured for home and contents insurance increased 7.2 percent of the year and 10.9 percent for commercial property insurance, pages 21 and 22.

Recommendation 18

That State and Territory governments exclude the cost of the GST for the purposes of calculating stamp duties on any other state or territory levies that are imposed on insurance premiums.

Recommendation 19

That governments avoid imposing on insurers levies and other taxes that cannot be passed on to policyholders (i.e. NSW Insurance Protection Tax).

4.3 Removing and preventing unnecessary regulatory burden in insurance

There are a number of further areas in which regulatory burden is in place or is proposed and which are the subject of Recommendations 20-27of this submission. Of these, Recommendation 20, that proposes tailoring dollar disclosure to general insurance is of greatest urgency.

4.3.1 FSR

ICA has welcomed the FSR Refinements announced by Parliamentary Secretary the Hon Chris Pearce, MP in May 2005. ICA is particularly encouraged by the acknowledgement that there is a need to "tailor" FSR to different products, including general insurance. ICA has had the opportunity to comment on draft amendments to the Corporations Act and is continuing to consult with Treasury in relation to these.

However, as ICA identified in its June 2005 response to the FSR Refinements package, there are a number of proposals that ICA believes could be developed further to complete the refinement process.

A key requirement of FSR, the dollar disclosure provisions,[25] has been overlooked in the FSR Refinements Proposals. Although the industry currently has the benefit of transitional relief from the provisions, this is due to expire in mid 2006.

The objective of the dollar disclosure provisions is to enhance consumer understanding and to help consumers compare products, especially between differing suppliers.

ICA supports the objective of the dollar disclosure provisions. However, the detail of the current provisions is such that they do not achieve their objectives for general insurance. This is a case in which "one size" of regulation simply cannot "fit all" general insurance. Although the provisions would provide useful disclosure in the context of investment products, they are likely to produce little, if any, benefit to consumers. To the contrary, the provisions are likely to produce disclosure that is *not meaningful for* consumers, is confusing and potentially misleading. These provisions will necessitate a significant review of PDSs, paragraphs and possibly pages of additional disclosure, the costs of which are inevitably passed on to consumers.

[25] The dollar disclosure requirements are contained in the Corporations Amendment Regulations (No 6) 2004 (Cth) (the dollar disclosure regulations), which were gazetted on 25 June 2004.

After consulting with ASIC and consumer representatives, ICA developed a proposal for solving the problem by "tailoring" dollar disclosure to general insurance.[26] Essentially, ICA believes that insurers should be able to meet the dollar disclosure provisions by disclosing dollars in their customised policy schedules and other ancillary documents rather than the PDS.

ICA's proposal for resolving dollar disclosure is currently under consideration by the Parliamentary Secretary Hon Chris Pearce, MP and Treasury. ICA recommends that its proposal for "tailoring" dollar disclosure to general insurance be adopted, as it will reduce unnecessary costs of compliance with regulation whilst retaining high levels of consumer protection.

Recommendation 20

That Regulations that are "tailored" to general insurance should be introduced to produce meaningful dollar FSR disclosure for general insurance products.

In addition to dollar disclosure, there are a number of ongoing extension issues under FSR. These are complex matters which have not been addressed in the FSR Refinements package, but which need careful consideration as the practical operation of FSR comes into clear view.

These extension issues include the definition of wholesale/retail clients[27] in the context of bundled general insurance products, cross endorsement, the impact of the FSR advice regime on the retail general insurance market, including the extent to which there has been a withdrawal of advice to retail clients. ICA believes that there is a clear case for FSR to be monitored on an ongoing basis in order to identify and assist in the resolution of issues that extend past the current FSR Refinements.

Recommendation 21

That Treasury monitor the ongoing operation of FSR, in order to identify and assist in the resolution of issues that extend past the current FSR Refinements.

4.3.2 APRA Stage 2 Reforms

In 2003, APRA commenced developing its latest raft of reforms to prudential standards (referred to collectively as "APRA Stage 2 Reforms"). A list of the APRA Stage 2 Reforms, together with their current status is set out in Appendix 3.

There are a number of areas where APRA Stage 2 Reforms to prudential standards create overlaps and inconsistency. In recent discussions with ICA, APRA has indicated its intention to reduce the areas of overlap and inconsistency in its forthcoming redraft of the prudential standards. ICA welcomes this approach from APRA and is currently working co-operatively and constructively with APRA to ensure that the prudential standards achieve an appropriate balance.

ICA's concern with the current drafts include:

- Duplication of corporate governance regulation. APRA Stage 2 Reforms include a proposal to regulate in the area of corporate governance. However, specific governance and other related requirements for corporations fall primarily under ASIC regulation and are laid out in the

[26] ICA "Proposal Paper: Tailoring Dollar Disclosure to General Insurance" (September 2005)

[27] "Retail" clients are individuals and small businesses under the FSR provisions

Corporations Act with its various amendments, including the most recent CLERP 9 reforms. Companies that are publicly listed are also required to adhere to the Australian Stock Exchange (ASX) *Principles of Good Corporate Governance and Best Practice*. In its proposed prudential standards, APRA also seeks to regulate corporate governance, including rules that are inconsistent with those set down by ASX and ASIC. Minor inconsistencies in wording between different regulations can create significant administrative problems and increased cost to general insurers with no benefit to policyholders.[28]

- Overlapping "fit and proper" requirements. Provisions for fit and proper persons are included in a number of different Australian regulations and legislation, in addition to those included in the proposed APRA Prudential Standards that form part of the Stage 2 Reforms. Considering only those applicable to financial services companies, there are organisational capacity requirements set by ASIC for Responsible Officers (as provided by the ASIC Guide (July 2003) of *Responsible Officers: Demonstrating compliance with organisational competency obligations)*, as well as the *ASX Principles of Good Corporate Governance*. APRA's proposed prudential standard on Fit and Proper would also govern the quality of persons in key positions within insurance companies. The proposed standards differ substantially from the criteria set down by ASIC and the ASX and APRA has determined not to recognise persons that have been approved as fit and proper by ASIC.

In addition to the current consultation on draft prudential standards, ICA looks forward to further opportunities to work with APRA at the early stages of developing new prudential standards. ICA believes that co-operative and constructive consultation at the early or developmental stages of new prudential standards should produce appropriate standards in a timely manner.

Consistent with Recommendation 2, such consultation should be focused on ensuring the most cost-effective means to achieve the stated policy intent. Consultation should be undertaken at all stages of the development of the regulations, including when policy is designed, standards are drafted and the legislation is translated into specific regulations and procedures applied by APRA.

4.3.3 ASIC regulatory projects

ASIC conducts a number of "campaigns" relating to insurance. These include "shadow shopping", reviews of financial services products sold by motor dealers and the proposed review of life time no claim bonuses for motor vehicle insurance.

In some instances, these reviews are conducted without full transparency as to whether there is a systemic basis for the campaign and the process by which the campaign will be conducted.

In some cases, such campaigns require insurers to expend significant resources on compliance, sometimes with statutory notices, including the production of documents. They require significant compliance and should, as in the case of regulation, be subject to cost-benefit assessment.

Recommendation 22

That ASIC should implement a transparent process whereby any proposed campaigns are subjected to a stringent cost benefit analysis prior to initiation.

[28] Refer to ICA submission "Prudential Supervision of General Insurance – Stage 2 Reforms: Finance and Risk Management, Corporate Governance, Fit & Proper" (August 2005)

4.3.4 Differing federal obligations for breach reporting – APRA/ASIC

Breach reporting is a compliance obligation that insurers are subject to under the Insurance Act and the Corporations Act. Yet, the threshold test for matters that must be reported are different under each Act, for reasons that are not entirely clear.

The Insurance Act requires an insurer to notify APRA as soon as practicable in writing if it becomes aware of a breach of a prudential standard or any other matter or occurrence that materially affects its financial position.[29] A failure to comply with this section is a criminal offence attracting penalty units for the individual or corporation concerned. All breaches, no matter how significant, must be reported.

Under the Corporations Act, an Australian Financial Services Licensee is only required to report a breach where that breach is "significant" having regard to five prescribed factors. ICA believes it is preferable to have this threshold in place and encourages the Government to undertake a review of the provisions of the Insurance Act that govern breach reporting.

Recommendation 23

That the Government undertake a review of the provisions of the Insurance Act that govern breach reporting.

4.3.5 Proposed amendments to the regulation of insurance contracts

During 2003-2004, an independent review panel undertook a thorough review of the IC Act. It made 38 recommendations for reform. The review of the IC Act also recommended the standard cover provisions of the Insurance Contracts Regulations be updated on the basis that these provisions have "not kept pace with market developments".[30]

Whilst ICA supports the majority of recommendations by the IC Act Review, ICA believes that the IC Act should not be amended unless:

- There is a proven problem with the operation of the IC Act;
- A proposed amendment would redress the problem;
- The costs and benefits for consumers have been thoroughly investigated through effective consumer testing; and
- The costs and benefits for insurers have been thoroughly investigated using appropriate modelling.

A careful cost benefit analysis should have particular regard to the level of consumer benefit of the recommendations on non disclosure, misrepresentations and utmost good faith, which are likely to have the heaviest compliance costs for industry.

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[29] Section 35A, *Insurance Act 1974*

[30] Review of the Insurance Contracts Act `984 "Final Report on Second Stage: Provisions other than section 54" at 46

In addition, appropriate transitional arrangements that take into account the interaction between the FSR Refinements and the IC Act and the impact on policy documentation should be considered.

Recommendation 24

That amendments to the IC Act, including the proposed update of the standard cover provisions, should not be initiated unless first subjected to a stringent cost benefit analysis that is informed by consumer testing.

4.3.6 Privacy Regulation – State/Federal overlaps and inconsistencies

The Privacy Act 1988 (Privacy Act) became applicable to the private sector in 2001. In general, ICA supports the Privacy Act and its members have found it to be a good example of light-touch regulation that has provided effective protection for consumers.

However, since 2001, insurers have witnessed a ballooning in privacy legislation, which has now developed into a "patchwork" of regulation in the States and Territories. In addition to the Office of the Federal Privacy Commissioner there are State Privacy Commissioners in multiple jurisdictions.

In some instances, a single piece of personal information, such as a name or an address, may have multiple pieces of legislation applying to it and multiple regulators to monitor and enforce compliance with that legislation.[31]

This is a particular problem and most obvious in the area of personal information that is defined as "health records", although this is but one of a number of areas where a "patchwork" has emerged. There are now inconsistencies between State legislation and the Privacy Act, additional obligations imposed by the State legislation over and above the Privacy Act and different obligations imposed by the State legislation.

The privacy "patchwork" adds to the regulatory burden. It requires legal advice to clarify the application of different legislation, staff time to respond to multiple regulators and to meet differing regulatory regimes.

The "patchwork" was acknowledged by the Privacy Commissioner in her 2004-2005 review of the private sector provisions of the Privacy Act. ICA strongly supports the Commissioner's recommendations to resolve this patchwork by clarifying jurisdictional issues and asking the Council of Australian Governments (COAG) to endorse national consistency in privacy related legislation.[32]

Recommendation 25

The Government should consider amending section 3 of the Privacy Act to remove any ambiguity as to the regulatory intent of the private sector provisions.

[31] Refer to findings of the Office of the Privacy Commissioner "Getting in on the Act: The Review of the Private Sector Provisions of the *Privacy Act 1988*" (March 2005)

[32] Office of the Privacy Commissioner "Getting in on the Act: The Review of the Private Sector Provisions of the Privacy Act 1988" (March 2005)

Recommendation 26

The Government should consider asking the Council of Australian Governments (COAG) to endorse national consistency in privacy related legislation.

4.3.7 Corporate Governance

In June 2005 the Corporations and Markets Advisory Committee (CAMAC) released two discussion papers, Corporate Duties Below Board Level (Below Board DP) and Personal Liability for Corporate Fault (Personal Liability DP), to which ICA responded in October 2005.

If implemented, the proposals set out in the Below Board DP would extend directors duties to an indefinite pool of management together with external consultants and contractors. This would further contribute to the compliance mentality that has emerged in corporations and would introduce a new definition of "senior management", in addition to those currently in place under the Corporations Act and APRA prudential standards. The Personal Liability DP includes a number of options for remodelling personal liability for corporate fault and expanding derivative liability which could have the effect of limiting risk taking and stifling innovation in the industry.

Recommendation 27

That no amendments to address the issues raised in the CAMAC May 2005 reports on extending corporate duties below board and extending derivative liability should be initiated unless first subjected to a stringent cost benefit analysis.

Appendix 1 – ICA Recommendations for improving the regulation of insurance

Review of financial sector regulation

1. Following the policy framework articulated in the Wallis Inquiry, the Government should be encouraged to adopt light-handed models of regulation in the major reviews of regulations currently under way. The implementation of these regulations, as for all regulation, should use the minimum level of market intrusion necessary to give effect to the identified policy objectives. It should be proportionate to the demonstrated market failure and applied efficiently.

Consultation

2. Consultation should be comprehensive focused on ensuring the most cost-effective means to achieve the stated policy intent of any new or substantially modified financial sector regulations be undertaken at all stages of the development of the regulations i.e. when policy is designed, legislation is drafted, and the legislation is translated into specific regulations and procedures applied by the relevant regulator.

3. The business community should continue to support a broad debate on the need for further microeconomic reform, with the development of well-designed regulations being an essential element of that agenda.

4. For major pieces of financial sector regulation, the Government should release a statement of policy intent, initially in the form of its 2nd reading speech and thereafter conduct a post implementation review within two years to measure whether the objectives were being achieved in the most cost effective manner.

Bureau of Financial Sector Regulation

5. A Bureau of Financial Sector Regulation should be established to oversee financial sector regulation.

6. The Bureau of Financial Sector Regulation should be tasked with the development of common methodologies to calculate the costs of complying with financial sector regulation. The Bureau should work closely with FICA (or the different industry associations) to help to ensure that this effort is as cost-effective as possible.

7. The Bureau of Financial Sector Regulation should be given a mandate to lift the quality of the cost-benefit analysis of financial sector regulation, and be resourced adequately for this task. The Bureau should encourage a deeper understanding of best practice regulation.

8. The Government should recognise the potential usefulness of regulated entities being able to develop their own compliance models to achieve regulator-specified outcomes. APRA and ASIC, in particular, should be encouraged to define what is expected of regulated entities and to develop a framework for alternative compliance models for specified areas of regulation.

9. The Reserve Bank should be encouraged to reconsider its current approach to the regulation of interchange and explore less constraining means to encourage appropriate competition.

10. The Bureau of Financial Regulation should have a mandate to monitor areas of duplication and inconsistency across regulators.

Place of Australia in global regulation

11. The Government should continue taking a lead in the developing of outcomes-based models of regulation in international forums. It should also encourage the recognition that regulatory frameworks may need to evolve as specific regulations are made operational. In adoption of international standards, Australian legislators and regulators should take due regard to the impact of early adoption on international competitiveness of domestic players.

Discretionary Mutual Funds and Direct Offshore Foreign Insurers

12. That the concept of 'carrying on insurance business in Australia', as set out in the Insurance Act, should be interpreted and applied so that all DMFs and DOFI providing protection for risks in the Australian market are regulated by APRA.

Federal prudential regulation

13. That the States and Territories not undertake any prudential regulation of general insurance.

14. That the States and Territories implement a process designed to reduce inconsistencies in their statutory schemes.

Policyholder Protection Scheme

15. That the Commonwealth Government introduce a systematic scheme to support the policyholders of insurance companies in the event of the failure of such a company, as part of the package of reforms of insurance regulation.

Insurance taxes

16. That state and territory governments abolish stamp duty on general insurance products.

17. That those states that have not already done so abolish fire services levies on insurers.

18. That state and territory governments exclude the cost of the GST for the purposes of calculating stamp duties on any other state or territory levies that are imposed on insurance premiums.

19. That governments avoid imposing on insurers levies and other taxes that cannot be passed on to policyholders (i.e., NSW Insurance Protection Tax).

Refining FSR

20. That Regulations that are "tailored" to general insurance should be introduced to produce meaningful dollar FSR disclosure for general insurance products.

21. That Treasury monitor the ongoing operation of FSR, in order to identify and assist in the resolution of issues that extend past the current FSR Refinements.

Breach reporting

21. That the Government undertake a review of the provisions of the Insurance Act that govern breach reporting.

ASIC

23. That ASIC should implement a transparent process whereby any proposed campaigns are subjected to a stringent cost benefit analysis prior to initiation.

Insurance contracts regulation

24. That amendments to the IC Act, including the proposed update of the standard cover provisions, should not be initiated unless first subjected to a stringent cost benefit analysis that is informed by consumer testing.

Privacy

25. The Government should consider amending section 3 of the Privacy Act to remove any ambiguity as to the regulatory intent of the private sector provisions.

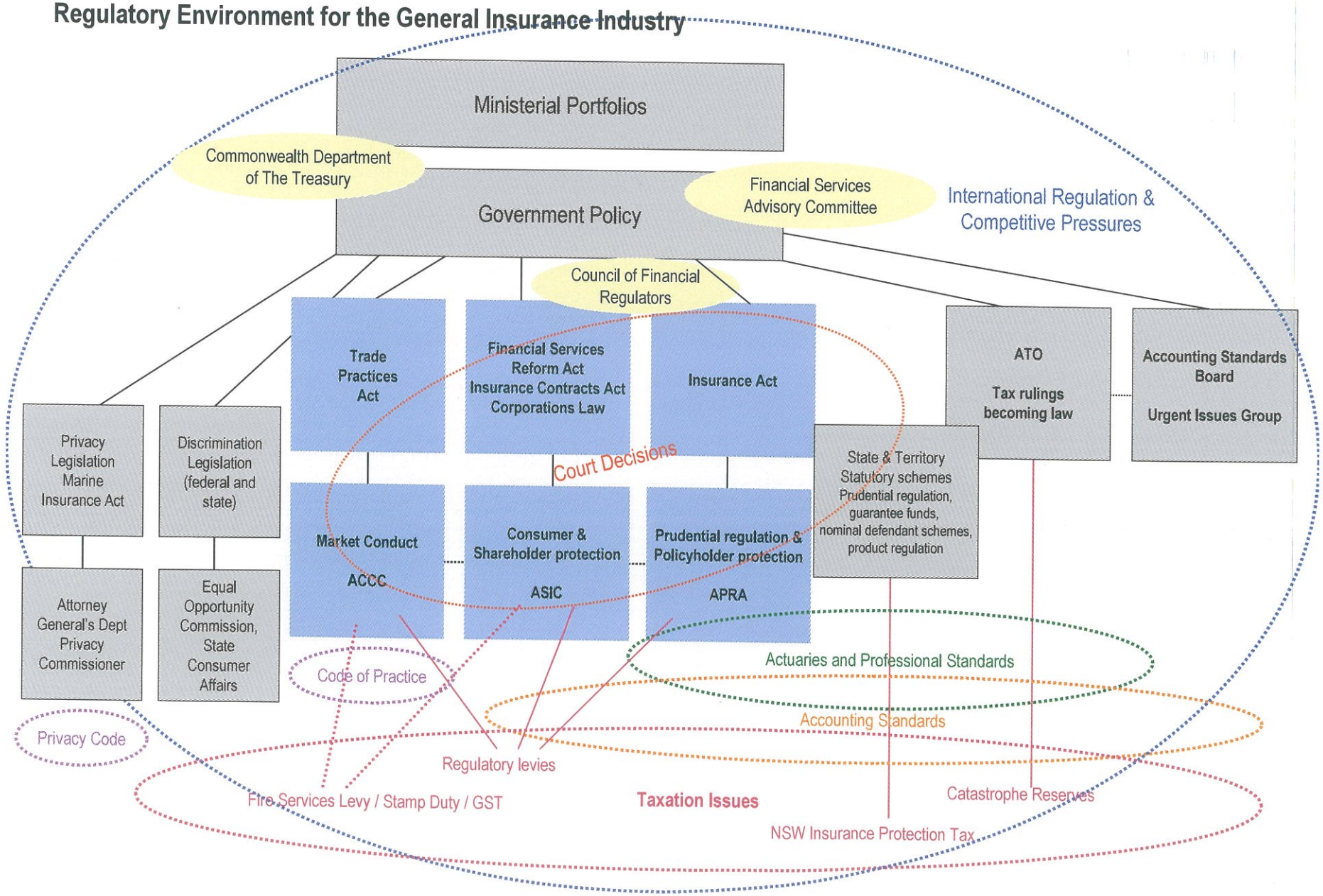
26. The Government should consider asking the Council of Australian Governments (COAG) to endorse national consistency in privacy related legislation.

Corporate Governance

27. That no amendments to address the issues raised in the CAMAC May 2005 reports on extending corporate duties below board and extending derivative liability should be initiated unless first subjected to a stringent cost benefit analysis.

Appendix 2 – Map of General Insurance Regulation

Regulatory Environment for the General Insurance Industry



Appendix 3 – Table of proposed reforms to general insurance regulation

Responsible Department or Regulator	Pending Reform	Regulatory impact on insurance	Status
APRA	Revised Draft Prudential Standards and Prudential Practice Guides on Risk Management	Replaces the existing prudential standard. Requires Board and senior management to approve and maintain a satisfactory Risk Management Framework.	Revised draft released November 2005. ICA and APRA working co-operatively and productively on achieving appropriate regulation.
APRA	Revised Draft Prudential Standards and Prudential Practice Guides on Outsourcing	Introduces a new standard for Boards to approve all material outsourcing arrangements.	Revised draft released November 2005. ICA and APRA working co-operatively and productively on achieving appropriate regulation.
APRA	Revised Draft Prudential Standards and Prudential Practice Guides on Reinsurance Management	Revises and expands the current standard imposing requirements on the documentation of reinsurance arrangements.	Revised draft released November 2005. ICA and APRA working co-operatively and productively on achieving appropriate regulation.
APRA	Revised Draft Prudential Standards and Prudential Practice Guides on Audit and Actuarial	Introduces new standards imposing a requirement to prepare an annual financial condition report and peer review for actuarial reports.	Revised draft released November 2005. ICA and APRA working co-operatively and productively on achieving appropriate regulation.
APRA	Second Draft Prudential Standard and Guidance Notes on Corporate Governance	Revises and expands the current standard imposing requirements for the governance of general insurers.	Second draft released May 2005. ICA expects a further draft to issue in January 2006.
APRA	Second Draft Prudential Standard and Guidance Notes on Fit and Proper	Revises and expands the current standard requiring insurers to have a policy for ensuring that responsible persons are fit and proper.	Second draft released May 2005. ICA expects a further draft to issue in January 2006.
APRA	Discussion Paper re Prudential Regulation of Corporate Groups.	Introduces a new standard covering the regulation of corporate groups including significant requirements regarding the concentration of risk.	ICA response made in October 2005
APRA	Adoption of IFRS Prudential Approach, Tier 1 Capital & Securitisation.	Introduces a new standard bringing APRA reposting into line with IFRS.	Discussion paper issued August 2005.
APRA	Draft Prudential Standards & Guidance Notes on Capital, Assets in Australia, Custodian Requirements	Introduces additional technical requirements on authorised insurers.	ICA currently being consulted by APRA as at the date of this submission.
Treasury	Corporations Amendment Regulations 2005 – refining the operation of Chapter 7 of the Corporations Act on the basis of the Government's May 2005 paper proposing a set of refinements to FSR.	Likely to increase regulatory burden in the short term as insurers review documents, systems and training in order to comply with proposed legislation, but should reduce costs of compliance in the long-term.	Expected 2005.

Responsible Department or Regulator	Pending Reform	Regulatory impact on insurance	Status
Treasury	Review and possibly amend Australia's product safety framework.	Implications for the affordability and availability of product liability insurance.	Productivity Commission currently consulting on this issue. ICA made a submission in 2005 identifying the possible implications for insurance.
Treasury	Trade Practices Legislation Amendment Bill (No 1) 2002 – a Bill to amend the TPA to implement the Dawson Review, including a notification process to facilitate collective bargaining by small businesses with large business.	Implications for the arrangements between insurers and smash repairers, amongst other small businesses that provide goods and services to insurers.	Following amendment in the Senate in October 2005, the Bill will return to the House of Representatives for further consideration.
Treasury	Proposed Financial Sector Legislation Amendment Bill 2006 to give effect to certain HIH Royal Commission recommendations and amend the Insurance Act 1973, the Financial Sector (Collection of Data) Act 2001 amongst others to enhance APRA powers. Further amendments will also be made to the scope of the Terrorism Insurance Act 2003.	Changes the powers of the prudential regulator of insurance, APRA.	Bill may be introduced during 2006.
Treasury	Proposed Financial Sector Legislation (Discretionary Mutual Funds and Direct Offshore Foreign Insurers) Amendment Bill 2006 to give effect to the recommendations of the Review of Discretionary Mutual Funds and Direct Offshore Foreign Insurers which the Government accepted in May 2004.	Possible modifications to the regulation of insurance and insurance-like business that is currently unregulated.	Expected to be completed and introduced following finalisation of the related prudential standard by APRA.
Treasury	Proposed General Insurance Supervisory Levy Amendment Bill	Modifies levies on insurers in order to cover funding for the National Claims and Policies Database.	Financial sector levies will be determined, announced and invoiced in the second quarter of 2006.
Treasury	Insurance Contracts Act Amendment Bill implementing the recommendations of the IC Act Review.	Involves significant new regulation for insurers, particularly with respect to proposed changes to the non-disclosure and misrepresentation provisions, and the amendments to the duty of utmost good faith. This may require amendments in training, systems, documents, contracts and other areas.	Consultation paper to be released 2006.
Treasury	ASIC (Enforcement Powers) Bill to change information gathering, investigative and enforcement powers of ASIC.	Changes the powers of the consumer protection regulator of insurance, ASIC.	Bill expected 2006.
CAMAC	Possible amendments to the Corporations Act with respect to "below board" duties and to Personal Liability for Corporate Fault	Implications for the affordability and availability of Directors and Officers insurance.	CAMAC consulting 2005.

Appendix 4 – Table of regulation of insurance by States and Territories

Queensland	Workers Compensation	▪ Government monopoly ▪ Regulatory functions removed from WorkCover to Q-Comp ▪ No direct private sector involvement ▪ No private sector involvement	CTP	▪ Private underwriters ▪ Regulatory and structural barriers to competition ▪ Very minor change after NCP review
NSW	Workers Compensation	▪ Public underwriting ▪ Privatisation in 1999 deferred, then cancelled ▪ McKinsey Review further entrenches role of WorkCover Authority ▪ Insurers will become contracted service providers to WorkCover	CTP	▪ Private underwriters ▪ Some capacity for competition ▪ Satisfied NCP tests
Victoria	Workers Compensation	▪ Public underwriting ▪ Privatisation from "appointed day" removed from legislation ▪ Insurers operate as contracted claims managers	CTP	▪ Public underwriting ▪ TAC is pure monopoly ▪ No effective change following NCP review
Tasmania	Workers Compensation	▪ Private underwriting and competitive ▪ Little restriction on competition	CTP	▪ Public underwriting ▪ MAIB is pure monopoly ▪ No effective change following NCP Review ▪ Pricing subject to review by GPOC
South Australia	Workers Compensation	▪ Public underwriting ▪ Insurers appointed as claims agents only ▪ No effective change following NCP review	CTP	▪ Public underwriting ▪ One insurer appointed as claims manager ▪ No effective change following NCP review
Western Australia	Workers Compensation	▪ Private underwriting ▪ Competitive market	CTP	▪ Public underwriting ▪ ICWA is pure monopoly ▪ No effective change following NCP review

ACT	Workers Compensation	▪ Private underwriting ▪ Competitive market	CTP	▪ Private underwriting ▪ One insurer only, others can apply to participate
Northern Territory	Workers Compensation	▪ Private underwriting ▪ Competitive market	CTP	▪ Public underwriting via TIO ▪ No private sector participation ▪ No change following NCP review

Source: ICA