INSURANCE COUNCIL OF AUSTRALIA

14 February 2020

The Manager
Redress and Accountability Unit
Financial System Reform Taskforce
The Treasury
Langton Crescent
PARKES ACT 2600

Dear Sir/Madam

FINANCIAL ACCOUNTABILITY REGIME

The Insurance Council of Australia[1] (Insurance Council) appreciates the opportunity to provide comments on the *Implementing Royal Commission Recommendations 3.9, 4.12, 6.6, 6.7 and 6.8 Financial Accountability Regime Proposals Paper* (**FAR Proposals Paper**) issued on 22 January 2020. We are also grateful for the opportunity to have participated in the Treasury co-ordinated Roundtable held on 3 February.

The Insurance Council acknowledges and supports the Government's intention to extend the Banking Executive Accountability Regime (**BEAR**) to APRA-regulated general insurers. We recognise the potential of the Financial Accountability Regime (**FAR**), if designed and implemented well, to increase the transparency and accountability of regulated general insurers. This will progressively improve entities' risk cultures and governance arrangements for prudential and conduct purposes. These outcomes, if achieved, would be a benefit to regulated general insurers and, most importantly, to their customers.

The FAR Proposals Paper outlines the intended structure and operation of the FAR. Many of the details of the regime's operation are to be determined at a later date. This will allow APRA and ASIC (**Regulators**), in their administration of the FAR, to more readily adjust system settings for subsequent changes in market practice.

However, this flexibility in the design of the FAR creates a higher than usual level of uncertainty at the outset for both the Regulators and regulated entities. This uncertainty is further heightened by the inclusion in the FAR, as compared to the BEAR, of market conduct

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[1] The Insurance Council of Australia is the representative body of the general insurance industry in Australia. Our members represent about 95 per cent of total premium income written by private sector general insurers. Insurance Council members, both insurers and reinsurers, are a significant part of the financial services system. September 2019 Australian Prudential Regulation Authority statistics show that the general insurance industry generates gross written premium of $49.5 billion per annum and has total assets of $128.3 billion. The industry employs about 60,000 people and on average pays out about $155.1 million in claims each working day.

Insurance Council members provide 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, professional indemnity insurance, commercial property, and directors and officers insurance).

as well as prudential matters, responsibilities shared between two regulators and an increase in the type of entities affected (most notably Non-Operating Holding Companies (**NOHCs**)). This may introduce a blurring of key concepts, confusion as to their scope (both individually and in combination) and uncertainty as to how they will apply in practice given different corporate structures and business models.

The Insurance Council suggests that there is a significant risk that the FAR reforms, if not implemented carefully, will lead to outcomes which hinder rather than benefit general insurers and, most importantly, their customers. Unintended consequences may include confused internal accountabilities, unnecessary organisational restructuring, a loss over time of innovation, unnecessarily subdued risk taking and a reduction in the general insurance sector's ability to attract executive talent both locally (when competing with industries not subject to the FAR) and globally in financial services markets.

All of these are significant risks. However, general insurers most acutely fear that over time it will become harder for them to recruit and retain senior executive talent. This risk arises not from any single feature of the FAR, but through the interplay of a number of factors. These include, for example, the deferred remuneration rules, the prohibition on employers paying or indemnifying relevant D&O insurance cover, a disproportionate extra-territorial effect and a possible disproportionate application of individual civil penalties. The skill areas with greatest vulnerability are IT, HR, Security and Fraud experts.

In order to mitigate these risks, the Insurance Council considers it important that the FAR legislation contain **a clear set of principles** to guide the Regulators in the development of detailed regulatory guidance and practices. The clear articulation of these principles will also assist regulated entities in their development of processes to comply with the regime.

These principles, which are further elaborated in Appendix 1, are:

1. The FAR only applies to senior executives.
2. The extra-territorial effect of the FAR is proportionate.
3. The FAR prevails where there is an inconsistency between a FAR standard and the standards of a regulator.
4. Enhanced compliance entities bear a greater compliance burden.
5. Penalties for individuals to be sought on a proportionate basis.

The FAR legislation should also prescribe a minimum six-month transition period with capacity for the Regulators to specify a later implementation date.

In Appendix 2, we list matters on which we seek written confirmation from Treasury that our understanding is correct.

In Appendix 3, we list matters on which further guidance is sought by general insurers either from Treasury or the Regulators.

The Insurance Council notes the explanation in the FAR Proposals Paper that the work on accountability for "end to end" product responsibility is ongoing. However, consistent with our submission to APRA (attached in Appendix 4), we are concerned that the broad scope and joint nature of the proposed product responsibility could create duplication which

undermines the FAR's objective of establishing a clear, transparent and common understanding within an institution of where accountability lies.

Too rigid a preoccupation with such an accountability may result in general insurers being forced to restructure organisations that are presently designed to facilitate the use of specialist technical expertise to support positive customer outcomes. Significant restructuring to meet the FAR would be an unnecessary regulatory cost and may have unintended and adverse impacts, including for customers.

The Insurance Council therefore considers that Treasury needs to develop a more precise definition of end to end product responsibility, one which more closely corresponds to product development, advice and sales and which also more closely aligns with existing operational structures of general insurers. This is consistent with our recommendations to APRA and the intent of the FAR.

Treasury verbally requested information at its Roundtable as to the extent of which general insurers utilised deferred consideration remuneration structures. Feedback from members, particularly those with global operations which have to compete on the international market for senior executive talent, is that deferred remuneration is widely used.

However, the feedback received has highlighted that the proposed $50,000 threshold would be too low and that a $100,000 threshold would be more appropriate at the senior executive level. An increase to the threshold to A$100,000 will mitigate the concern associated with deferring immaterial amounts over an extended period of time.

If you have any questions or comments in relation to our submission please contact John Anning, the Insurance Council's General Manager Policy, Regulation Directorate, on telephone: 02 9253 5121 or email: janning@insurancecouncil.com.au.

Yours sincerely

Robert Whelan
Executive Director & CEO

INSURANCE COUNCIL OF AUSTRALIA

APPENDIX ONE

PRINCIPLES TO BE INCLUDED IN DRAFT LEGISLATION

1. The FAR only applies to senior executives

The BEAR utilises both a principles-based element and a prescriptive element to identify accountable persons. The principles-based element is framed around the concepts of "effective management" or "control". Use of those concepts is apt when focused on prudential matters and when supplemented with a limited number of prescribed accountable persons. In that context, the test broadly correlates with identifying those persons with responsibility for setting the strategic, business and compliance direction and frameworks for a business. These are persons which our members would ordinarily regard as senior executives.

The FAR utilises this BEAR framework to identify accountable persons, but then expands it to include conduct matters; a more diverse range of industries and entities; and a larger number or prescribed persons each described as "senior executive responsib[le] for" a function, business etc. It is also contemplated that more than one person may hold a particular responsibility. The FAR Proposals Paper does not define the term "senior executive".

The Insurance Council has significant concerns that this stretching of the BEAR approach to identifying accountable persons for use in a FAR context may lead to a large number of persons who our members would not regard as senior executives being identified as accountable persons under the FAR. The Insurance Council notes oral statements made by both Treasury and APRA at the 3 February roundtable that it is not intended that the FAR apply to middle management.

However, the Insurance Council considers there is a risk that both the regulator and regulated entities when applying this layered approach in complex organisations with multiple reporting lines, identify individuals as accountable persons who are more sensibly regarded as middle management.

To mitigate that risk, the Insurance Council considers:

- the FAR legislation should contain a strong and unambiguous statement of principle that the FAR only applies to senior executives;
- the Explanatory Memorandum to the FAR legislation should contain guidance, including a set of indicia, to distinguish between a senior executive and a middle manager; and
- the FAR should allow sufficient flexibility for conglomerates with multiple FAR entities to determine where accountability appropriately sits, so as not to unduly enforce the cascading of accountability in large complex organisations.

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2. The extra-territorial effect of the FAR is proportionate

As a matter of practice, statutes are normally not drafted to have extra-territorial effect. This accords with the legal notion of sovereignty and the regulatory practicalities of enforcement. The BEAR departs from convention and has extra-territorial effect. The Insurance Council understands, for example, that the BEAR obligations are cascaded down to persons resident in New Zealand and identified as accountable persons under the BEAR. The Insurance Council is not aware of the reasons as to why this approach was taken in the BEAR. However, we presume it was due to the particular circumstances and structure of the banking industry.

The FAR, in contrast to the BEAR, applies to a wider range of industries and to a wider range of entities. The impact of a blanket extra-territorial approach is likely to result in a competitive disadvantage in attracting and retaining talent in overseas markets. We are also concerned that this introduces a layering of multiple and potentially inconsistent regulatory requirements between Australia and overseas. These factors will increase complexity and drive up the cost of compliance for FAR entities without a proportionate benefit to Australian consumers.

The Insurance Council is of the view that as a matter of principle the FAR should not have an extra-territorial effect unless the Regulators can demonstrate that the Australian prudential and conduct benefit outweighs the burden imposed in applying the regime to specific industries and/or classes of entities. For instance, the Insurance Council recognises there may be specific circumstances where it is appropriate that the FAR apply to a limited number of individuals resident outside Australia. This may be the case where these non-resident persons have responsibility for significant overseas operations of an Australian FAR entity, whether conducted through a branch or subsidiary, which significantly impacts the FAR entity. However, the Insurance Council is of the strong view that the scope of the FAR should not cascade further into, and capture, other non-resident persons and foreign operations of FAR entities.

The Insurance Council suggests that a proportionate extra-territorial approach which retains a clear focus on senior executives and outcomes for Australian consumers be adopted. This approach will also help avoid a proliferation of accountable persons, with the associated diffusion of accountabilities away from the most senior executives in a FAR entity; an outcome which would be inconsistent with the intent of the FAR.

3. The FAR prevails where there is an inconsistency between a FAR standard and the standards of a regulator

The stated purpose of the FAR in the FAR Proposals Paper is to

> *"extend this [BEAR] responsibility and accountability framework across all APRA regulated industries. In doing so, the FAR is intended to increase the transparency and accountability of entities in these industries and improve risk culture and governance for both prudential and conduct purposes."*[2]

[2] Page 2, FAR Proposals Paper

The Insurance Council understands that the FAR legislation will establish the framework (including the principles and obligations) and that the Regulators will have the powers to prescribe details for several aspects of the FAR. We recognise that this will provide flexibility in the ongoing administration of the FAR.

We understand that the Treasury and the Regulators are working closely in development of the FAR. We are, however, concerned that there is the potential for the details of the regime as prescribed by the Regulators, and as yet not known by general insurers, to be inconsistent with the intent and framework of the FAR legislation. For example, the FAR Proposals Paper includes deferred remuneration requirements that are expected to be less stringent than those to be determined by APRA in the revised Prudential Standard CPS 511: Remuneration.

The Insurance Council considers this approach to be unnecessarily risky in the circumstances. The Insurance Council recommends, to minimise the potential risk of inconsistency between the FAR legislation and matters prescribed by the Regulators, that the FAR legislation contain provisions which require:

- the dual regulators to consult with one another and Treasury as to whether proposed regulatory guidance conflicts with the FAR legislation; and
- in the event of a conflict, or inconsistency, the FAR legislation prevails.

4. Enhanced compliance entities experience a greater compliance burden

The BEAR envisaged a graduated compliance and penalty burden depending upon a relevant entity's classification as a small, medium or large ADI. This classification system has not been retained in the FAR. The FAR classifies entities as either "core compliance entities" or "enhanced compliance entities".

The only consequence which follows from classification of an entity under the FAR as an enhanced compliance entity is imposition of the requirement to submit and update accountability maps and statements. The FAR Proposals Paper states:

> *"Since the BEAR commenced on 1 July 2018, industry feedback suggests that the development, submission and updating of accountability maps and statements poses a significant compliance burden on smaller entities … Classifying entities into core compliance entities and enhanced compliance entities is intended to reduce the compliance burden for the majority of entities."*[3]

Member feedback to the Insurance Council is that entities will have to prepare accountability maps and statements to ensure that they comply with their obligations under the FAR regime. Accordingly, our industry's perception is that the removal of the subsequent obligation to submit these maps and statements to the regulators will do little to reduce the compliance burden for the majority of entities. They would like to see the FAR include measures which have a substantive effect on reducing the compliance burden for the majority of general insurers.

[3] Page 4, FAR Proposals Paper

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5. Penalties for individuals to be sought on a proportionate basis

The Insurance Council recognises the Government's intent that breaches under this regime attract the highest penalties. We also note statements by Treasury at the Roundtable that penalties are intended to apply in a graduated manner and that the Regulators will only seek penalties for significant breaches.

Members of the Insurance Council have significant concerns that a possible unintended consequence of the FAR is that it will become increasingly difficult for general insurers to recruit and retain talent, as compared to other industries and other jurisdictions. This would clearly have a long-term deleterious impact on the industry.

In this context and given the downside risk to the industry and consumers, the Insurance Council considers that Treasury's expectations in this regard as to how the Regulators will act should be elevated to a principle in the FAR legislation.

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APPENDIX TWO

TREASURY CONFIRMATION OF INSURANCE COUNCIL UNDERSTOOD MATTERS

1. Prohibition on entities paying the cost of insuring accountable persons against the consequences of breaching the FAR

The FAR Proposals Paper indicates that *"As under BEAR, entities will be prohibited from indemnifying or paying the cost of insuring accountable persons against **the consequences** of breaching the FAR."* [4] (emphasis added)

The Insurance Council understands from Treasury that breaches of the FAR by entities are intended to attract the highest penalties and that penalties imposed on individuals are intended to be graduated. This is the context in which it is proposed that entities be prohibited from indemnifying or paying the cost of insuring accountable persons.

Under the BEAR, there is an exemption to this prohibition in relation to an entity indemnifying or paying the cost of insuring accountable persons in relation to a liability to legal costs. This exemption is based on section 37KA of the *Banking Act 1959*.

There is significant concern amongst Insurance Council members that this exemption will not be retained in the FAR. This stems from the reference to "the consequences" in the text cited above. Removal of this exemption is likely to have a substantive impact on the availability, affordability and scope of Directors & Officers Insurance for accountable persons.

The Insurance Council understands that Treasury intends that this exemption will be retained in the FAR. Given the importance of the issue to members and its potential market impacts, the Insurance Council requests Treasury's written confirmation that this exclusion does not apply to legal and other defence costs which a person may be liable for or otherwise incur.

2. Accountable persons of a group may be accountable persons for an insurer

For general insurance groups that are a "Level 2" APRA-regulated group, and also comprise "Level 1" regulated general insurer(s), the FAR Proposals Paper does not restrict an accountable person for the NOHC (or head of the Level 2 Group) from being an accountable person for the Level 1 insurer(s). We understand from Treasury that this is a deliberate design feature of the FAR.

The Insurance Council supports this approach as it enables FAR entities to assess and determine the individuals who have responsibility for particular responsibilities appropriate to their organisational and governance structures and seeks written confirmation of this.

[4] Page 9, FAR Proposals Paper

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3. Applicability of each particular responsibility

The Insurance Council notes that not all of the particular responsibilities may be relevant to APRA regulated entities which are required to identify an accountable person in respect of them. This is particularly relevant for NOHCs.

The Insurance Council suggests that it would be helpful for the FAR legislation to clarify that if a particular responsibility is not relevant for a FAR entity, the entity is not required to allocate an accountable person to that particular responsibility. The Insurance Council would appreciate written confirmation on this point.

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APPENDIX 3

ISSUES ON WHICH FURTHER GUIDANCE IS SOUGHT

The below is a list of issues on which members of the Insurance Council seek guidance in relation to operation of the FAR. In providing this list, the Insurance Council recognises that it may be some time before Treasury and/or the Regulators are able to provide guidance on some of the matters in the list. Nonetheless, the Insurance Council thought it would be of assistance to Treasury to identify these issues now.

1. It is uncertain how civil penalties under the FAR will interact with civil penalties under other pieces of legislation e.g. section 912A of the Corporations Act. This causes complexity.
2. There is a potential mismatch between an entity's existing breach reporting obligations, e.g. to ASIC under the Corporations Act and APRA under other legislation, and the FAR. How do these obligations interact with those under the FAR?
3. The notification obligations require reporting of all instances of a failure to comply with the obligation of the FAR, which may extend to notifications of breaches of licensing obligations. As noted under 2. above there may be a potential mis-match between breach reporting and it may be useful to introduce a "materiality" threshold, at least for conduct-related licensing matters.
4. How do the obligations of the accountable person for particular responsibilities apply to roles with statutory obligations, for example the appointed actuary? Such roles may be held by an individual who is not a senior executive.
5. Guidance is needed on how Treasury intends to ensure that APRA only uses its powers to veto appointments on a reserve basis.
6. A metric of 'total assets' for the purposes of distinguishing between core and enhanced compliance entities needs to be developed.
7. How will the proposed threshold of total assets work practically in the context of divestments and acquisitions?
8. Will entities need to inform the regulators when a change in total assets causes them to move from a core to enhanced compliance entity and vice versa.
9. What is the transition period for entities whose compliance entity status changes?
10. There is a need for early regulatory guidance as to what constitutes "significant" or "substantial" subsidiaries to enable general insurers to plan adequately for the FAR's introduction.
11. A general observation is that members strongly believe guidance is required around the requirements to identify an accountable person so that an appropriate accountable person can be identified and not just any accountable person. This is particularly difficult for those examples in the indicative list which identify an accountable person by using the words "responsibility" and "management" in the same sentence, or where there are overlapping responsibilities between items. Further specific comments on the indicative list are made in subsequent items.

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12. Some of the list of particular responsibilities overlap e.g. between end-to-end product responsibility and remediation responsibility, remediation responsibility and service responsibility. This is commented upon in the body of the submission letter and Appendix Two.
13. In respect of the proposed new responsibility for the setting of incentives (including incentives for staff and outward facing incentives, such as, loyalty programmes) we would welcome clarity on the responsibility as it applies to staff incentives. For example, is this intended to apply to the executive that proposes the incentives framework to the Board for approval?
14. Also in relation to the responsibility for incentives, typically across the general insurance industry, we would expect different accountable persons to be responsible for the setting of incentive frameworks for the entity's staff, third party distributors of the entity's products or services and customer incentives. It would be helpful to clarify whether this responsibility may be held by different accountable persons in respect of each of these and other relevant incentive types.
15. In respect to the proposed new responsibility for management of client or member remediation programmes (encompassing hardship considerations where relevant), there may be, similar to incentives, different accountable persons responsible for these programmes in respect of different products and services. It would also be helpful to clarify whether this responsibility can be held by different accountable persons in respect of each different product or service.
16. How will the process for accountability work where the person responsible for the remediation programmes is not a senior executive, as commonly understood, and therefore that person should not be subject to the FAR? Is the next person up the corporate hierarchy the accountable person?
17. There should be better identification of the accountable person for a NOHC given that these perform very specific functions, such as, investing in subsidiaries, lending initial or on-going financial support, protecting assets, absorbing financial losses etc.
18. We would welcome clarity around the roles that apply to APRA and ASIC entities, noting that a NOHC is not subject to ASIC requirements.
19. We would welcome clarification as to the definition of variable remuneration. For example, does this include retention grants? Signing-on bonuses? Also see our comments on variable remuneration in the body of the submission letter.
20. It is unclear how the deferred remuneration obligations will apply to persons who may temporarily fill the position of an accountable person.
21. The FAR Proposals Paper does not refer to all of the deferred remuneration requirements as currently included in the BEAR. Can we assume that these additional requirements will lapse? Or do they remain unchanged?
22. We understand that the intention is to create stand-alone legislation for the FAR. That is, the provisions establishing the FAR regime will not be included in relevant industry legislation, such as the *Insurance Act 1973*. We suggest that it would be useful if related concepts and definitions contained in industry legislation or relevant prudential standards be replicated, or incorporated by reference, into the FAR legislation. A good example is the definition of "prudential matters" and "fit and proper".

23. We would welcome further clarification on appropriate approaches to particular responsibilities that clearly do not relate to a “function” or single aspect of an entity’s operations. That is, it may be appropriate to identify a framework owner as the relevant accountable person for a particular responsibility, rather than be required to identify all accountable persons with responsibility for complying with frameworks/policies as jointly holding the prescribed responsibility.

INSURANCE COUNCIL OF AUSTRALIA

APPENDIX FOUR

23 August 2019

Ms Heidi Richards
General Manager, Policy Development
Policy and Advice Division
Australian Prudential Regulation Authority
Level 12, 1 Martin Place
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Dear Ms Richards

THE BANKING EXECUTIVE ACCOUNTABILITY REGIME – PRODUCT RESPONSIBILITY

The Insurance Council of Australia[5] (Insurance Council) appreciates the opportunity to comment on APRA's proposed approach to product responsibility under the Banking Executive Accountability Regime (BEAR). Although the proposals are currently aimed at ADIs, the Insurance Council's submission highlights some of the issues that should be considered when BEAR is extended to general insurers.

The Financial Services Royal Commission (FSRC) received evidence of IT systems and processing errors that resulted in the inadvertent overcharging of fees. It highlighted two reasons for those errors: the number and complexity of products; and the absence of 'end-to--end' accountability. In that context, Commissioner Hayne formulated recommendation 1.17:

> After appropriate consultation, APRA should determine for the purposes of section 37BA(2)(b) of the Banking Act, a responsibility, within each ADI subject to the BEAR, for all steps in the design, delivery and maintenance of all products offered to customers by the ADI and any necessary remediation of customers in respect of any of those products.

The Insurance Council and its members support reforms that address the issues raised in the FSRC around the lack of accountability for processing and administrative errors. However, we are concerned that the broad scope and joint nature of the proposed product

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[5] The Insurance Council of Australia is the representative body of the general insurance industry in Australia. Our members represent approximately 95 percent of total premium income written by private sector general insurers. Insurance Council members, both insurers and reinsurers, are a significant part of the financial services system. June 2019 Australian Prudential Regulation Authority statistics show that the general insurance industry generates gross written premium of $48.4 billion per annum and has total assets of $128.4 billion. The industry employs approximately 60,000 people and on average pays out about $151.4 million in claims each working day.

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responsibility could create duplication that undermines the BEAR's objective of establishing a clear, transparent and common understanding within an institution of where accountability lies.

Scope and nature of accountability

The Insurance Council and its members do not support APRA's proposed broad interpretation of what is in scope of end-to-end accountability. Instead, we submit that a narrow definition that more closely aligns with product development, and advice and sales would better reflect the operational structure of insurers, and provide clear and transparent accountability consistent with the intention of the BEAR.

The proposed product responsibility should be consistent with the principles of the BEAR

As an underlying principle, the BEAR recognises that different business structures may be used. Consequently, the legislation provides the scope and flexibility for entities to determine the most appropriate allocation of accountable persons to its business activities.[6] Specifically, under the BEAR an entity must have an accountable person for "all parts or aspects of the operations of the relevant group"[7] and an entity's accountability map must contain sufficient information to identify that accountable person.[8] As noted in the Revised Explanatory *Memorandum to the Treasury Laws Amendment (Banking Executive Accountability and Related Measures) Bill 2017*:

> The combination of key personnel obligations and the accountability maps will operate to let an ADI satisfy itself and show APRA that it has allocated all key personnel obligations to accountable persons and that those accountable persons can discharge their obligations under the BEAR. This will demonstrate full coverage of the ADI group by accountable persons without the need to have an accountable person individually responsible for every single subsidiary, for example (1.62)

By analogous reasoning, we suggest that the requirement to have an accountable person with end-to-end responsibility for each product that an entity offers to its customers may be superfluous. In particular, we note that the requirements under the BEAR "ensure that there is accountability for all parts or aspects of the group's business"[5] and would appear to address the issues raised in the FSRC relating to the lack of accountability for administrative and processing errors.[9] To the extent that there are identified gaps in accountability, these could be addressed on an individual basis taking into account the operational structure of an entity's business.

A broad interpretation of the scope of end-to-end responsibility leads to duplication and potentially dilutes accountability

Section 37BA of the *Banking Act 1959* provides for specific, accountable persons covering a range of responsibilities. For example, s37BA(3)(f) refers to information management,

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[6] Paragraphs 1.56 and 1.57, Revised Explanatory Memorandum to the *Treasury Laws Amendment (Banking Executive Accountability and Related Measures) Bill 2017*

[7] s37D *Banking Act 1959*

[8] ss37F and 37FB *Banking Act 1959* [5] Paragraph 1.13, Revised Explanatory Memorandum to the *Treasury Laws Amendment (Banking Executive Accountability and Related Measures) Bill 2017*

[9] We note that the evidence presented at the FSRC largely predates the implementation of the BEAR.

including information technology systems. APRA's proposed approach that end-to-end product responsibility extend to "linkages to IT systems and data quality" creates duplication of accountability. This duplication is at odds with the BEAR's objective of establishing a clear, transparent and common understanding within an institution of where accountability lies.

Similarly, the proposed broad scope of accountability has the potential to conflict with existing dispute resolution principles. For example, under ASIC's *Regulatory Guide 165 Licensing: Internal and external dispute resolution*, responsibility for investigating complaints should be separated from staff involved in the subject matter of the complaint.

To minimise duplication, we submit that a narrower interpretation of end-to-end product responsibility is more appropriate. This could align more closely with the Government's reforms to introduce product design and distribution obligations by focusing on product development, and advice and sales.

A broad interpretation raises practical difficulties

Many of the Insurance Council's members are structured along functional lines so as to facilitate effective spans of control and allow specialist technical expertise to be employed across the product life cycle. Key functions include: product design, pricing and underwriting; product distribution; and claims management. *All* parts of an enterprise should be oriented to better customer outcomes and understand the part they play in the customer value chain to achieving those outcomes. In applying the proposed product responsibility framework to insurers, care needs to be taken to avoid dictating organisational designs which undermine both individual accountability and collective responsibility. It may also introduce practical inefficiencies and misalignment, for instance, replicating the claims function by product line would introduce barriers to the exchange of best practice across products, and would also create inconsistent practices across an insurer.

In addition, the imposition of a broad, vertical, end-to-end product responsibility creates practical difficulties in identifying individuals with an adequate skill set to take accountability for all stages of the product life cycle. For example, a chief actuary will be skilled to assess the integrity of product design and pricing, but not necessarily the customer claims experience. Many insurers mitigate the risk of poor accountability at the product level by introducing processes to ensure that cross-functional review of products occur. These processes have been given sharper focus by reforms to introduce product design and distribution obligations to ensure there is regular review of product performance against a set of metrics, including important indicators of customer outcome and experience.

Extent of 'end-to-end' responsibility and third parties

APRA's proposed approach to product responsibility appears to leave open the question of whether an accountable person in one entity should be accountable for the actions of third parties. As an example, insurers may participate in syndicates to offer insurance to customers. In this example, would an accountable person in one entity be held accountable for the actions of other members of the syndicate? Similarly, in a claims handling context, insurers often engage external suppliers (builders, restorers, smash repairers). APRA's

proposed approach to product responsibility for these elements should be consistent with Treasury's reforms aimed at treating claims handling as a financial service.[10]
APRA proposes that white-label or other branded products be included within the scope of end-to-end responsibility. However, further details are needed to assess how this might work in practice.

Coverage of products

Need greater clarity on the definition of 'product'

In its proposed approach to product responsibility, APRA does not provide a definition of 'product'. Is it limited to 'financial products' as defined in Chapter 7 of the *Corporations Act 2001*? Would, for example, roadside assistance services offered by insurers be captured by APRA's proposed regime?

If you have any questions or comments in relation to our submission, please contact John Anning, the Insurance Council's General Manager Policy, Regulation Directorate, on (02) 9253 5121 or janning@insurancecouncil.com.au.

Yours sincerely

Robert Whelan
Executive Director and CEO

[10] See: https://treasury.gov.au/consultation/c2019-t364638