

24 November 2020

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By email: maryanne.hinwood@apra.gov.au

Dear Ms Hinwood

APRA 2019-20 Financial Year Self-Assessment for External Validation

Thank you for your letter and attachments of 2 November. The Insurance Council of Australia (**Insurance Council**)¹ appreciates the opportunity to comment on APRA's 2019-20 Financial Year Self-Assessment under the Regulator Performance Framework (**RPF**).

We understand from Attachment 1 to your letter that the purpose of this consultation is to act as "a sounding board" for APRA's self-assessment, in particular whether its "conclusions are reasonable, objective or excessively positive" and if "the areas identified for further improvement are appropriate or justified".

APRA has self-assessed itself as meeting each of its six KPIs:

- KPI 1: Regulators do not unnecessarily impede the efficient operation of regulated entities;
- KPI 2: Communication with regulated entities is clear, targeted and effective;
- KPI 3: Actions undertaken by regulators are proportionate to the regulatory risk being managed;
- KPI 4: Compliance and monitoring approaches are streamlined and coordinated;
- KPI 5: Regulators are open and transparent in their dealings with regulated entities; and
- KPI 6: Regulators actively contribute to the continuous improvement of regulatory frameworks.

¹The Insurance Council is the representative body of the general insurance industry in Australia. ICA 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. 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). July 2020 Australian Prudential Regulation Authority statistics show that the general insurance industry generates gross written premium of \$51.4 billion a year and has total assets of \$135.4 billion. The industry employs about 60,000 people and on average pays out about \$171.1 million in claims each working day. Over the 12 months to July 2020 the industry's net profit after tax (NPAT) was \$1.0 billion – a 70.5 per cent decrease from the prior year's NPAT of \$3.5 billion. The industry's underwriting result was \$1.4 billion, falling by 39 per cent from \$2.3 billion in the prior year.

The COVID-19 global pandemic has created significant challenges for Australia's financial services sector, both for regulators and regulated entities. In that context, the Insurance Council's overall assessment is that APRA has performed creditably in its regulation of the general insurance industry. APRA acted early, decisively, and appropriately when on 23 March it suspended for six months the majority of its planned policy and supervisory initiatives. The decision enabled businesses to focus on supporting their customers during this period.

At the time of this decision, general insurers were still operating at or near full capacity to service customers after a series of major natural catastrophes, including the black summer bushfires. Multiple public enquiries into those fires and natural national disasters more broadly have found that the general insurance industry's performance in assisting affected policy holders through those catastrophes has been very good. And as those challenges gave way to yet more issues that had to be addressed because of COVID-19, APRA's regulatory approach has enabled the industry to maintain that high consumer service standard.

The Insurance Council also has found when dealing with APRA officials that they consistently conduct themselves in a professional, considered, and transparent manner.

In relation to the specific KPIs, the Insurance Council:

- agrees that APRA's conclusions that it met KPIs 2-6 are reasonable, objective and not excessively positive; but
- questions whether APRA's conclusion in relation to KPI 1 is not unduly positive. This is because the primary evidence advanced by APRA to support its assessment is not readily apparent to non-government external stakeholders and is inconsistent with the results of the biennial survey.

Detailed observations are provided in Appendix 1.

Going forwards, the Insurance Council observes that the 2021 biennial stakeholder survey would benefit from tighter drafting of the questions to ensure that they more clearly align with the KPIs on which APRA assesses its performance. There were several questions asked in the 2019 biennial stakeholder survey, the results of which were put forward as evidence in the 2019-20 self-assessment, where the connection is somewhat tenuous. These are highlighted in Appendix 1.

We trust that our observations are of assistance. If you have any questions or comments in relation to our submission please contact John Anning, the Insurance Council's Head, Regulatory Policy, on telephone: 02 9253 5121 or email: janning@insurancecouncil.com.au.

Yours sincerely



Andrew Hall
Executive Director and CEO

EXTERNAL STAKEHOLDER VALIDATION COMMENT

KPI 1: Regulators do not unnecessarily impede the efficient operation of regulated entities

The criterion which APRA uses to demonstrate that it has met “its commitment to analysing the costs, benefits and impacts of proposed changes” is “by achieving 100 per cent compliance with Office of Best Practice Regulation (OBPR) requirements”. Whether this conclusion is reasonably objective or excessively positive is difficult to assess for a non-Commonwealth government external stakeholder.

The Insurance Council understands that the OBPR plays an important intra-government role in the approval process for legislative instruments. However, it is not clear to the Insurance Council what role the OBPR plays, if any, in assessing whether the 5 updated prudential standards, the 3 practice guides and 4 reporting standards issued by APRA unnecessarily impede the efficient operation of regulated entities. Further, it is not clear whether 100% compliance is merely expected, or an indicator of excellence. As a result, it is not clear to the Insurance Council whether this is the correct criterion with which to assess APRA’s performance against this KPI.

This lack of clarity as to the suitability of this criterion would seem to be supported by APRA’s biennial stakeholder survey in which 76% of external stakeholders were either neutral, disagreed or strongly disagreed with the proposition that “changes to APRA’s prudential framework sufficiently consider the costs of regulation imposed on industry”.

The Insurance Council therefore does not consider that it is in a position to assess whether APRA has met this KPI (given the criterion selected), but suggests that APRA’s assessment is overly positive (given the results of the external stakeholder survey).

The Insurance Council considers that an area for further improvement is the development of a criterion for KPI 1 which enables non-government external stakeholders to assess APRA’s self-assessment of its performance as against that KPI.

KPI 2: Communication with regulated entities is clear, targeted, and effective

In relation to general insurance we note that the general insurance standards and guidance section of the APRA website was accessed 37,153 times during the 2019-20 FY. Further, 25 speeches were made during this period, although it is not clear how many of those speeches related to general insurance. The Insurance Council does note the importance of Mr Summerhayes speech of 20 October 2020 to the Australian Business Roundtable for Disaster Resilience and Safer Communities webinar (see further comments below).

APRA also refers to the public consultations conducted, of which 9 were completed during the year – a lower than usual number due to COVID-19. Answers to questions asked in the biennial stakeholder survey show a very high degree of satisfaction with the quality of the technical rulings and guidance produced by APRA.

The Insurance Council agrees that the technical content produced by APRA is clear, targeted and effective, although the Insurance Council also observes that it might be a challenge for

APRA to continue to meet that standard as its guidance expands beyond readily quantifiable areas (such as capital adequacy) to more subjective areas (such as the suitability of remuneration policies).

Nonetheless, the Insurance Council considers it important that APRA continue to take positions on areas and issues which previously were not thought of as relating to APRA's core functions, but which nonetheless have a material impact on regulated entities. Given its relevance to insurance affordability, the 20 October 2020 speech by Mr Summerhayes which highlighted issues, such as the need for increased government infrastructure investment in disaster mitigation works rather than the existing expenditure bias towards disaster clean-up works, is a good example.

The Insurance Council considers that APRA's assessment that it has met this KPI to be reasonable, objective and is not excessively optimistic.

KPI 3: Actions undertaken by regulators are proportionate to the regulatory risk being managed

APRA notes that, in light of the COVID-19 global pandemic, it redirected the attention of frontline supervisors to how financial institutions were responding to COVID-19, particularly in the areas of financial and operational resilience. APRA also highlights that in January 2020 it publicly released its first annual statement of regulator priorities, which is a welcome development (it is also an example of "clear, targeted and effective" communication). APRA also refers to the roll-out of its new Supervision Risk and Intensity Model (SRI) which was subject to a useful webinar on 20 November.

The Insurance Council considers that the operation of the SRI will be central to whether APRA's actions in relation to the regulatory risk being managed in the general insurance sector are proportionate going forwards. In relation to the 2019-20 FY, the Insurance Council has not received any feedback from members that the operation of the outgoing PAIRS and SOARS systems had resulted in any disproportionate actions by APRA.

The Insurance Council considers that APRA's assessment that it has met this KPI to be reasonable, objective and is not excessively optimistic. This is consistent with 90% of respondents to the biennial survey agreeing or strongly agreeing that APRA is primarily risk-based in its supervision.

KPI 4: Compliance and monitoring approaches are streamlined and coordinated

APRA refers to its strengthened working relationships with other regulators, notably the Council of Financial Regulators, and establishment of a dedicated regulatory affairs team. It notes that it collects data on behalf of other government agencies and refers to targeted data collections, including in relation to general insurance a one-off collection on business interruption exposure. The biennial survey question was whether "the information that APRA collects in the course of supervision is adequate to assess risks in your entity." The question does not go to whether APRA asked for that information in a streamlined and coordinated way.

Member feedback to the Insurance Council is that there is "a high level of liaison with other regulators (ASIC, RBNZ, FINMA) by APRA, resulting in streamlined and coordinated monitoring".

The Insurance Council considers that APRA's assessment that it has met this KPI to be reasonable, objective and is not excessively optimistic.

KPI 5: Regulators are open and transparent in their dealings with regulated entities

APRA notes that due to the rapidly deteriorating operating environment triggered by the COVID-19 global pandemic that it promptly reset priorities and directed resources to key risks and vulnerabilities. APRA refers to meeting more than 100 government and private organisations, including the Insurance Council, during FY 2019-20. The biennial stakeholder survey shows strong agreement with the proposition that APRA is consultative in its supervision and less definitive agreement that APRA is timely in resolving requests, the latter question not relating to the openness or transparency of APRA's dealings with regulated entities.

In the Insurance Council's experience, APRA officials make themselves available to engage with the Insurance Council and its members and conduct themselves in an open and transparent manner. For example, the ICA asked APRA if the capital relief extended to ADIs in relation to loan deferrals announced on 23 March would also apply to LMI provisions for COVID-19 affected loans. After consideration, APRA advised that relief would not be extended to LMIs. APRA officials met with the Insurance Council and its LMI members, they explained APRA's reasoning, answered questions and concluded the matter with formal written advice. The Insurance Council considers that this issue was professionally managed by APRA.

The Insurance Council agrees that APRA's assessment that it has met this KPI to be reasonable, objective and is not excessively optimistic.

KPI 6: Regulators actively contribute to the continuous improvement of regulatory frameworks

APRA notes its expanded and strengthened engagement with domestic and international peer agencies. The Insurance Council is unable to comment on this particular point. APRA also notes that it has broadened stakeholder engagement mechanisms, including initiating webinars one of which an Insurance Council employee attended on 20 November. The question asked in the biennial stakeholder survey was whether APRA's consultation packages provide a good basis for consultation with industry, for which there was a strong agreement.

The Insurance Council considers that APRA's assessment that it has met this KPI to be reasonable, objective and is not excessively optimistic.