

25 October 2012

General Manager
Financial System Division
The Treasury
Langton Crescent
PARKES ACT 2600

By email: safefinancialsector@treasury.gov.au

Dear Sir or Madam

Submission regarding General Insurance

Following the informal consultations on 11 October 2012 I wish to make this formal submission on the consultation paper 'Strengthening APRA's Crisis Management Powers'.

Note that the submission is in respect of GENERAL INSURANCE companies only.

There are five points made in this submission:

1. The desirability of having a voluntary mechanism (like the Business Transfer Act) that APRA can apply to general insurance companies to transfer blocks of business for distressed companies and companies in run-off.
2. Disagreement with the proposal regarding reinsurance in 9.2.4
3. Comments on the interim period of notional insurance cover.
4. Submission against the inclusion of Ministerial approval.
5. Difficulties with the Group powers.

Business Transfers

The Financial Sector (Business Transfer and Group Restructure) Act should be amended to include Voluntary Transfers for General Insurers.

At present a major impediment to APRA dealing effectively with a struggling general insurer is that it is virtually impossible to organise for another insurer to take over the business. The only mechanism is a Scheme under the Insurance Act which takes at least

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six months and carries a significant cost in legal and actuarial fees and client communications, or a Compulsory Transfer that can only come too late in the piece.

Many general insurers are currently in run off (i.e. no longer writing business) but there is no practical mechanism to close them down and transfer the remaining outstanding claims to another authorised insurer.

Based on a quick read there is nothing in Part 3 of the Business Transfer Act (dealing with Voluntary Transfers) that would be a problem for general insurance business.

If you would like more detail on the arguments for this change or to discuss its implications I would be happy to oblige.

Reinsurance Proposal in 9.2.4

The only issue that arises with the current application of s116A(1) is additional cost for insurers and reinsurers, with no gain to prudential supervision.

The 'arms length' reinsurance market has an unquestioned record for remitting reinsurance recoverables in an orderly manner. Given that a broker is accountable to the insurer (not the reinsurer) then remitting funds to a broker is legally sound.

The 'fortress Australia' approach that APRA has taken to reinsurance is unhelpful and costly and should be pared back on a risk-based assessment process.

My suggestion would be that for the 'arms length' market the requirements be reviewed and rationalised, while for the 'non arms length' market collateralisation be used as the principal prudential measure.

The Interim Period of Notional Insurance Cover

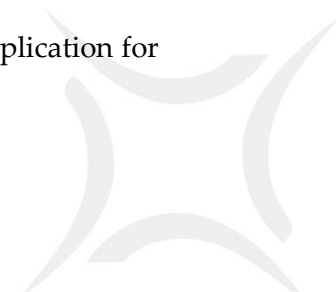
For general insurance, the provision of an interim period of notional insurance cover is desirable. In my view, however, a blanket extension to 90 days is too generous.

While acknowledging the additional complexity, my suggestion would be as follows:

- The interim period should end 28 days after the policy expiry or 6 weeks after the receipt of an offer for renewal, whichever is the later
- For policies that have not expired, APRA may extend the interim period up to 90 days depending on the circumstances.

Ministerial Approval

I support the proposal in Section 6.1.1 to automatically activate the FCS on application for winding up of a general insurer.



Difficulties with the Group Powers

I do not support extending the general insurance powers to a NOHC, or to subsidiaries of the general insurer or the NOHC. My reasons for this view are:

- Authorisation and direct supervision of a NOHC or subsidiaries is overly complex, rarely clear in its boundaries and ultimately not assured of success
- Effective supervision of the 'ring-fencing' aspects of the general insurance regime is a superior approach, which includes arrangements by which group companies may provide essential services.

I realise this is a complex area, and is just as relevant for APRA's supervision in normal circumstances. Therefore I have not included more detail in this submission, but would be happy to discuss further if requested.

Overall Comments

With the large number of relevant laws it is difficult to analyse what the outcomes would be unless one has been through actual experiences. Therefore I support in general the Treasury approach of listening carefully to APRA's difficulties with previous experiences and responding accordingly.

With general insurers I am aware of a problem with a company going into voluntary administration and several problems with priority over reinsurance recoveries. If these problems can be ironed out it would be good progress.

With any proposal to significantly strengthen APRA's powers there are likely to be concerns over accountability of APRA. It is not unknown for a regulator to make an incorrect or ineffective decision, and given that the survival of businesses is at stake there would be a high cost if APRA were to act inappropriately. Having made this observation, I do not believe that any 'before the event' accountability check should be included because it is more likely to cause unnecessary delay that will make the situation worse. Therefore despite some unease I believe the best compromise is to bring APRA to account after the action if that proves necessary. It is important to understand who has that role, given that the aggrieved corporation will be in no position to do so.



About the Author

Finity is an independent firm of actuaries and consultants specialising in the general insurance sector. Members of the firm have acted as an Inspector for APRA on several occasions, as well as supporting the HIH Royal Commission. The author spent a year working at APRA during a sabbatical and also has advised regulators in some other countries under contract from multi-national agencies.

Yours sincerely

A handwritten signature in black ink, appearing to be 'Geoff Atkins', with a long horizontal flourish extending to the right.

Geoff Atkins

