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Dear Mr Grummitt

### **GPS 110: BOARD RESPONSIBILITY FOR ADEQUACY OF CAPITAL**

The Insurance Council of Australia (Insurance Council) is writing to raise concerns that members have expressed about the requirement that a Board “ensure” that the regulated entity’s capital is adequate having regard to its risk profile. The issue is that satisfaction of this responsibility cannot be guaranteed in practice and is therefore inappropriate. The basis of this view is set out below.

#### **Board requirement**

The requirement is set out in the following documents (with our emphasis in bold):

- Prudential Standard GPS 110, Summary:  
*The ultimate responsibility for the prudent management of capital of a general insurer or Level 2 insurance group rests with its Board of directors. The Board **must ensure** that the general insurer or Level 2 insurance group maintains an adequate level and quality of capital commensurate with the scale, nature and complexity of its business and risk profile, such that it is able to meet its obligations under a wide range of circumstances.*
- Prudential Standard GPS 110, paragraph 6:  
*As a consequence of the key role played by capital in the financial strength of a regulated institution, the Board of a regulated institution **must ensure** that the regulated institution has capital that is adequate for the scale, nature and complexity of its business and its risk profile, such that it is able to meet its obligations under a wide range of circumstances.*
- Prudential Practice Guide CPG 110, paragraph 1:  
*Under the capital standards, the Board of a regulated institution has primary responsibility for the capital management of that institution. This obligation goes beyond the **need to ensure compliance** with regulatory capital requirements and requires the Board **to ensure** that each regulated institution holds capital resources commensurate with its risk profile.*

- Prudential Practice Guide CPG 110, paragraph 7:  
*An ICAAP involves an integrated approach to risk management and capital management, based around assessing the level of, and appetite for, risk in the regulated institution and **ensuring** that the level and quality of capital is appropriate to that risk profile.*
- Prudential Practice Guide CPG 110, paragraph 16:  
*Under the capital standards, a regulated institution may make use of a group ICAAP or components of that ICAAP. In doing so, the Board of each regulated institution in the group is still required **to ensure** that the ICAAP is appropriate and meets the requirements of the capital standards in relation to the institution.*

You will be aware that the word “ensure” is uniformly taken to mean “to make sure or to make certain”. However, the Board of an insurer is not in a position to make sure or certain that the requirement set out above is satisfied. Even the most expert Board could not “ensure”, for instance, that an insurer has adequate capital commensurate with the scale, nature and complexity of its business and risk profile, or that the insurer complies with all regulatory capital requirements.

The Insurance Council therefore considers that to place such a requirement on a Board is unrealistic and should be reconsidered. The Insurance Council submits that the obligation could be easily recast as something achievable without endangering the substance of the provisions in GPS 110 and CPG 110. It is suggested that the requirement as set out in GPS 110 and CPG 110 be revised along the lines of:

“The Board of the general insurer or Level 2 insurance group will take reasonable steps to maintain an adequate level and quality of capital commensurate with the scale, nature and complexity of its business and risk profile, such that it is able to meet its obligations under a wide range of circumstances.”

If you require further information in relation to this submission, please contact Mr John Anning, Insurance Council’s General Manager Policy – Regulation Directorate at [janning@insurancecouncil.com.au](mailto:janning@insurancecouncil.com.au).

Yours sincerely



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Executive Director & CEO