

23 August 2019

Ms Heidi Richards
General Manager, Policy Development
Policy and Advice Division
Australian Prudential Regulation Authority
Level 12, 1 Martin Place
SYDNEY NSW 2000

Dear Ms Richards

THE BANKING EXECUTIVE ACCOUNTABILITY REGIME – PRODUCT RESPONSIBILITY

The Insurance Council of Australia¹ (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 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.

¹ 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.

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).

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.² Specifically, under the BEAR an entity must have an accountable person for "all parts or aspects of the operations of the relevant group"³ and an entity's accountability map must contain sufficient information to identify that accountable person.⁴ 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.⁶ 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, 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

² Paragraphs 1.56 and 1.57, Revised Explanatory Memorandum to the *Treasury Laws Amendment (Banking Executive Accountability and Related Measures) Bill 2017*

³ s37D *Banking Act 1959*

⁴ 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*

⁶ We note that the evidence presented at the FSRC largely predates the implementation of the BEAR.

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.⁷

⁷ See: <https://treasury.gov.au/consultation/c2019-t364638>

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