

Banking, Insurance, Life Insurance and Health Insurance (prudential standard) determination No. 1 of 2022

Superannuation (prudential standard) determination No. 3 of 2022

EXPLANATORY STATEMENT

Prepared by the Australian Prudential Regulation Authority (APRA)

Banking Act 1959, section 11AF

Insurance Act 1973, section 32

Life Insurance Act 1995, section 230A

Private Health Insurance (Prudential Supervision) Act 2015, section 92

Superannuation Industry (Supervision) Act 1993, section 34C

APRA may, in writing, determine, vary or revoke a prudential standard that applies to an APRA-regulated institution under:

- (1) subsections 11AF(1) and (3) of the *Banking Act 1959* (Banking Act), which applies to all authorised deposit-taking institutions (ADIs) and authorised non-operating holding companies (authorised banking NOHCs);
- (2) subsections 32(1) and (4) of the *Insurance Act 1973* (Insurance Act), which applies to all general insurers and authorised non-operating holding companies (authorised insurance NOHCs);
- (3) subsections 230A(1) and (5) of the *Life Insurance Act 1995* (Life Insurance Act), which applies to all life companies, including friendly societies, and non-operating holding companies (registered life NOHCs); and
- (4) subsections 92(1) and (5) of the *Private Health Insurance (Prudential Supervision) Act 2015* (PHIPS Act), which applies to all registered private health insurers.
- (5) subsection 34C(1) and 34C(6) of the *Superannuation Industry (Supervision) Act 1993* (SIS Act), which applies to all Registered Superannuation Entity Licensees (RSE licensees)

On 16 November 2022, APRA made the following determination instruments (collectively the Instruments):

- Banking, Insurance, Life Insurance and Health Insurance (prudential standard) determination No. 1 of 2022, which revokes *Prudential Standard CPS 510 Governance* made under Banking, Insurance, Life Insurance and Health Insurance determination No. 2 of 2019 and determines a new *Prudential Standard CPS 510 Governance* (CPS 510); and

- Superannuation (prudential standard) determination No. 3 of 2022, which revokes *Prudential Standard SPS 510 Governance* made under Superannuation (prudential standard) determination No. 1 of 2016 and determines a new *Prudential Standard SPS 510 Governance* (SPS 510).

The instruments commence on 1 January 2023.

1. Background

APRA's mandate is to ensure the safety and soundness of prudentially regulated financial institutions so that they can meet their financial promises to depositors, policyholders and superannuation fund members within a stable, efficient and competitive financial system.

APRA carries out this mandate through a multi-layered prudential framework that encompasses licensing and supervision of entities. The Banking Act, Insurance Act, Life Insurance Act, PHIPS Act and SIS Act allow APRA to issue legally binding prudential standards that set out specific prudential requirements with which APRA-regulated entities must comply.

In 2021, APRA determined a new *Prudential Standard CPS 511 Remuneration* (CPS 511) which sets out requirements to ensure that APRA-regulated entities maintain remuneration arrangements that provide appropriate incentives to individuals to prudently manage the risks they are responsible for, and that there are appropriate consequences for poor risk outcomes. CPS 511 commences on 1 January 2023.

With the commencement of CPS 511 on 1 January 2023, a number of existing requirements relating to remuneration, including those detailing requirements in relation to Board Remuneration Committees and Remuneration policies, currently set out in CPS 510 and SPS 510, will become redundant as these matters will be covered by new requirements in CPS 511.

2. Purpose and operation of the instruments

The purpose of Banking, Insurance, Life Insurance and Health Insurance (prudential standard) determination No. 1 of 2022 is to revoke the existing requirements under CPS 510 for banking and insurance and replace it with the new CPS 510 which incorporates necessary consequential amendments resulting from the commencement of CPS 511. The amendments apply to:

- ADIs and authorised banking NOHCs that are significant financial institutions (SFIs) as defined in APRA's definitions prudential standards, or a group headed by such an ADI or authorised banking NOHC from 1 January 2023; and
- general insurers, life companies and private health insurers that are SFIs, groups headed by such entities and groups headed by authorised insurance NOHCs, parent entities of Level 2 insurance groups or registered life NOHCs that are SFIs from 1 July 2023.

The purpose of Superannuation (prudential standard) determination No. 3 of 2022 is to revoke the existing requirements under SPS 510 for superannuation and replace it

with the new SPS 510 which incorporates necessary consequential amendments resulting from the commencement of CPS 511. The amendments apply to RSE licensees that are SFIs from 1 July 2023.

This reflects the fact that CPS 511, while commencing on 1 January 2023, will apply in stages to different types of APRA-regulated entities.

Where CPS 510 refers to an Act, Regulation, prudential standard or Australian Accounting Standard, this is a reference to the document as it exists from time to time, and which is available on the Federal Register of Legislation at www.legislation.gov.au. Where CPS 510 refers to the APES 110 Code of Ethics for Professional Accountants, it is a reference to that document as it exists from time to time and which may be freely used (available from the Accounting Professional & Ethical Standards Board (APESB) at <https://apesb.org.au>). The APESB is an independent, national body that sets the code of ethics and professional standards with which accounting professionals who are members of CPA Australia, CA ANZ or IPA must comply.

Where CPS 510 refers to the ASX Corporate Governance Council's Corporate Governance Principles and Recommendations (2nd Edition 2007), it is a reference to that document as it exists from time to time and which may be freely used (available from the ASX Corporate Governance Council at www2.asx.com.au). ASX stands for Australian Securities Exchange. ASX is an integrated exchange offering listings, trading, clearing, settlement, technical and information services, technology, data and other post-trade services. It acts as a market operator, clearing house and payments system facilitator. It oversees compliance with its operating rules, promotes standards of corporate governance among Australia's listed companies and helps to educate retail investors.

The standards provide for APRA to exercise various discretions. Decisions made by APRA exercising those discretions are not subject to merits review. This is because these decisions are preliminary decisions that may facilitate or lead to substantive decisions which are subject to merits review.

Under the Banking Act, Insurance Act, Life Insurance Act and PHIPS Act, a breach of a prudential standard is a breach of the enabling legislation, as each enabling Act provides that regulated entities must comply with the standard. Under the SIS Act, it is a condition on all RSE licences that the RSE licensee must comply with the RSE licensee law, which includes prudential standards. However, there are no penalties prescribed for breach of the prudential standards under any of these Acts. Instead, an entity's breach of the enabling legislation is grounds for APRA to make further, substantive decisions under the relevant enabling legislation in relation to the entity. Those decisions may include the decision:

- (a) to issue a direction to the regulated entity, including a direction to comply with the whole or part of a prudential standard (section 11CA of the Banking Act, section 104 of the Insurance Act, section 230B of the Life Insurance Act, section 131D of the SIS Act); and a direction to comply with all, or specified obligations, which includes prudential standards (section 96 of the PHIPS Act); and

(b) to revoke an authority to carry on banking business (section 9A of the Banking Act); a banking NOHC authorisation (section 11AB of the Banking Act); an authority to carry on insurance business (section 15 of the Insurance Act); an insurance NOHC authorisation (section 21 of the Insurance Act); registration of life insurance business (section 26 of the Life Insurance Act); a life NOHC authorisation (section 28C of the Life Insurance Act); or to revoke an authority to operate an APRA-regulated superannuation fund (section 29G of the SIS Act).

It is only at this stage that an entity is exposed to a penalty: loss of licence or imposition of a penalty if it breaches the direction (50 penalty units each day under section 11CG of the Banking Act, section 108 of the Insurance Act; section 230F of the Life Insurance Act; 30 penalty units each day under section 104 of the PHIPS Act; and 100 penalty units each day under section 131DD of the SIS Act).¹ In nearly all cases,² the decisions are preceded by a full consultation with the regulated entity to raise any concerns they may have in relation to the decision.

The decisions of APRA to impose a direction are subject to merits review (subsection 10(1) of the SIS Act, section 11CA of the Banking Act, section 104 of the Insurance Act, section 236 of the Life Insurance Act, section 168 of the PHIPS Act), which is appropriately available at the point where an entity could be exposed to a penalty.

All decisions to revoke authorisations/registrations under the SIS Act, Banking Act, Insurance Act and Life Insurance Act are subject to merits review, unless specifically excluded by the enabling legislation.

Revocation of an authorisation to carry on banking business or a banking NOHC authorisation is subject to merits review unless either:

- (a) APRA has determined that access to natural justice and merits review is contrary to the national interest or contrary to the interests of depositors with the body corporate; or
- (b) (in the case of ADIs only) the authority is an authority that is to cease to have effect on a day specified in the authority (section 9A(8) of the Banking Act).

Revocation of an authorisation to carry on insurance business or an insurance NOHC authorisation is subject to merits review (ss 15 and 21 of the Insurance Act).

Revocation of registration as a life insurance company or a life NOHC authorisation is subject to merits review (section 236 of the Life Insurance Act). The situation in relation to cancellation of registration under the PHIPS Act is different to the other enabling legislation.

¹ Section 54B of the SIS Act also provides that breach of a covenant under sections 52 or 52A is a civil penalty provision. The covenants include a requirement to comply with prudential standards in relation to specified topics (conflicts, capital requirements for operational risk, MySuper and choice products).

² The Banking Act, Insurance Act and Life Insurance Act specifically provide that APRA does not need to consult where APRA is satisfied that doing so could result in a delay in revocation that would be contrary to the national interest or the interests of depositors with the body corporate (subsection 9A(4) of the Banking Act), contrary to the national interest (subsection 15(4) of the Insurance Act), or contrary to the public interest (subsection 26(5) of the Life Insurance Act), respectively. Consultation is not specifically required under the SIS Act.

Exemption from sunseting and disallowance

SPS 510 is exempt from disallowance in accordance with section 44(2)(b) of the *Legislation Act 2003* (Legislation Act) and regulation 9 of the *Legislation (Exemptions and Other Matters) Regulations 2015* (Legislation Regulations) as SPS 510 is an ‘instrument (other than a regulation) relating to superannuation’.³ SPS 510 is exempt from sunseting in accordance with section 54(2)(b) of the Legislation Act and regulation 11 of the Legislation Regulations as this Legislative Instrument is ‘an instrument (other than a regulation) relating to superannuation’.⁴

Incorporation by reference

Where SPS 510 refers to provisions in the Act, this is a reference to the Act as it exists *from time to time*, and which is available on the Federal Register of Legislation at www.legislation.gov.au. Where SPS 510 refers to another superannuation prudential standard, the superannuation standard referred to is the version that exists *at the time* this Instrument is determined. Where SPS 510 refers to the APES 110 Code of Ethics for Professional Accountants, it is a reference to that document that existed at the time this instrument was determined.

3. Consultation

These consequential changes were set out in various public consultation papers APRA issued as part of its consultation on new remuneration requirements. These included:

- Discussion paper - Strengthening prudential requirements for remuneration, APRA, July 2019;
- Response paper – Strengthening prudential requirements for remuneration, APRA, 12 November 2020;
- Response paper – Strengthening prudential requirements for remuneration, APRA, August 2021

No comments were received in submissions to the consultation on these consequential amendments.

4. Regulation Impact Statement

The Office of Best Practice Regulation advised that no Regulation Impact Statement was required as the changes to the standards are minor and machinery.

³ For paragraph 44(2)(b) of the Legislation Act, section 42 of the Legislation Act (disallowance of legislative instruments) does not apply to a legislative instrument in a class of legislative instrument referred to in an item of the table contained in regulation 9 of the Legislation Regulations. Item 3 of the table contained in regulation 9 of the Legislation Regulations provides that ‘an instrument (other than a regulation) relating to superannuation’ is a class of legislative instrument not subject to disallowance.

⁴ For paragraph 54(2)(b) of the Legislation Act, Part 4 of Chapter 3 of the Legislation Act (sunseting of legislative instruments) does not apply to a legislative instrument in a class of legislative instruments referred to in an item of the table contained in regulation 11 of the Legislation Regulations. Item 6 of the table contained in regulation 11 of the Legislation Regulations provides that ‘an instrument (other than a regulation) relating to superannuation’ is a class of legislative instrument not subject to sunseting.

5. Statement of compatibility prepared in accordance with Part 3 of the Human Rights (Parliamentary Scrutiny) Act 2011

A Statement of compatibility prepared in accordance with Part 3 of the *Human Rights (Parliamentary Scrutiny) Act 2011* is provided at Attachment A to this Explanatory Statement.

ATTACHMENT A

Statement of Compatibility with Human Rights

Prepared in accordance with Part 3 of the *Human Rights (Parliamentary Scrutiny) Act 2011*

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The Legislative Instruments (the instruments) are compatible with the human rights and freedoms recognised or declared in the international instruments listed in section 3 of the *Human Rights (Parliamentary Scrutiny) Act 2011* (HRPS Act).

Overview of the Legislative Instrument

The purpose of Banking, Insurance, Life Insurance and Health Insurance (prudential standard) determination No. 1 of 2022 is to revoke the existing requirements under CPS 510 for banking and insurance and replace it with the new CPS 510 which incorporates necessary consequential amendments resulting from the commencement of CPS 511. The amendments apply to:

- ADIs and authorised banking NOHCs that are significant financial institutions (SFIs) as defined in APRA's definitions prudential standards from 1 January 2023; and
- to general insurers, life companies, private health insurers, groups headed by such entities that are SFIs and groups headed by authorised insurance NOHCs, parent entities of Level 2 insurance groups or registered life HOHCs from 1 July 2023.

The purpose of Superannuation (prudential standard) determination No. 3 of 2022 is to revoke the existing requirements under SPS 510 for superannuation and replace it with the new SPS 510 which incorporates necessary consequential amendments resulting from the commencement of CPS 511. The amendments apply to RSE licensees that are SFIs from 1 July 2023.

Human rights implications

APRA has assessed these instruments and is of the view that they do not engage any of the applicable rights or freedoms recognised or declared in the international instruments listed in section 3 of the HRPS Act. Accordingly, in APRA's assessment, the instruments are compatible with human rights.

Conclusion

The instruments are compatible with human rights as they do not raise any human rights issues.