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Preamble

Following a recommendation by the HIH Royal Commissioner that the Insurance Act 1973 be amended to extend prudential regulation to all discretionary insurance-like products, the Government commissioned the Potts Review in 2004.

After a series of consultations with industry, on 3 May 2007 the Minister for Revenue and Assistant Treasurer announced that discretionary mutual funds (DMFs)\(^1\) would be required to provide data so that the Government could better understand their use and operation. The announcement indicated that within three years of the start of this collection regime the Government would consider whether prudential regulation of DMFs is necessary.

The Government has amended the Financial Sector (Collection of Data) Act 2001 (FSCODA) to require DMFs to provide detailed data to the Australian Prudential Regulation Authority (APRA) on their operations. These amendments to FSCODA are contained in the Financial Sector Legislation Amendment (Discretionary Mutual Funds and Direct Offshore Foreign Insurers) Act 2007 (DMF Act), which was introduced to Parliament on 21 June 2007 and passed on 13 September 2007.

The purpose of this discussion paper is to give DMFs an understanding of the type of data APRA proposes to collect and seek submissions on these proposals. The proposed forms are attached to this paper and available at www.apra.gov.au.

Submissions

Written submissions and queries on APRA’s proposals should be emailed to DMF_Reporting@apra.gov.au for the attention of Keith Chapman, General Manager Policy Development. The closing date for submissions is Friday, 2 November 2007.

APRA will consider all submissions received and use the responses to assess whether any modifications to the proposals should be made. APRA intends to finalise its reporting requirements for DMFs by January 2008. The requirements will apply to all DMFs that are in existence on or after 30 June 2008.

Submissions will be treated as public unless clearly marked as confidential and the confidential information contained in the submission is identified. Submissions may be the subject of a request for access made under the Freedom of Information Act 1982 (FOIA). APRA will determine such requests, if any, in accordance with the provisions of the FOIA.

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\(^1\) The Government’s legislation, and APRA’s proposals, apply to DMFs other than those that operate solely within a State or Territory and which are established under a State or Territory statute.
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Glossary

APRA
Australian Prudential Regulation Authority

ASIC
Australian Securities and Investments Commission

DMF
Discretionary mutual fund as defined in the DMF Act. Refer to the extract of the legal definition in the DMF Definition.

In plain English, DMFs are entities that offer ‘discretionary cover’, that is, an insurance-like product that may involve an obligation on the DMF to consider meeting a claim made on it, but gives the DMF a discretion as to whether it will pay the claim. A DMF may be a trust, mutual, company limited by guarantee or other structure.

DMF Act
Financial Sector Legislation Amendment (Discretionary Mutual Funds and Direct Offshore Foreign Insurers) Act 2007

D2A
Direct to APRA software which is used for submission of APRA forms.

FOIA
Freedom of Information Act 1982

FSCODA
Financial Sector (Collection of Data) Act 2001

Claim
Payment or set of payments sought by a member from the DMF to reimburse the member for a loss.

Contribution
The payment that a DMF member makes to a DMF to secure the right to discretionary cover. It is like an insurance premium but is not a premium because the DMF is not an insurance company.

Member
The party that purchases discretionary cover and pays contributions to the DMF. A member is like an insured, but is not an insured because a DMF is not an insurance company.

Premium
Payment made by a DMF to an insurance company to purchase an insurance policy to protect the DMF against large individual claims or against a large aggregation of claims.

Recovery
Payment made to a DMF by an insurance company arising from the insurance policy taken out by the DMF with the insurance company.
Background

On 3 May 2007, the Minister for Revenue and Assistant Treasurer announced the Government’s approach to the regulation of DMFs. This announcement was followed by the DMF Act which was passed on 13 September 2007. The Act is not intended to apply to DMFs that operate solely within a State or Territory and that are established under a State or Territory statute.

At this time, and in the absence of appropriate data, the Government has decided that DMFs will not be subject to prudential regulation. However, DMFs will be subject to a compulsory data collection regime so that the Government can better understand their use and operation. Holders of an Australian Financial Services Licence (AFSL) will be required to provide data to the Australian Securities and Investments Commission (ASIC) on their dealings in products provided by DMFs, with specific requirements to be set after further consultation by ASIC.

APRA’s Proposals

Introduction

The Minister for Revenue and Assistant Treasurer’s announcement indicated that the Government will, within three years of the start of the data collection regime, consider whether prudential regulation of DMFs is necessary. All DMFs will be required to provide data to APRA under FSCODA, which makes it compulsory for DMFs to provide information to APRA.

This discussion paper is accompanied by APRA’s proposed Notification Form, Static Information Form and reporting forms and instructions for DMFs, and seeks detailed submissions on the content.

APRA will release final reporting requirements following consideration of submissions. DMFs may enter email addresses in “APRA Subscriptions” on the bottom right hand side of www.apra.gov.au. Select “Advanced Subscription Options” and under “Subscription Categories” tick “Non-Regulated entities” to receive filtered notifications. Select “Advanced Subscription Options” and under “Subscription Categories” tick “Non-Regulated entities” to receive filtered notifications.

DMF Definition

APRA’s proposals apply to entities that are DMFs, as defined in the DMF Act. An extract from the DMF Act states that:

“(5) A discretionary mutual fund is a fund (however constituted) for making payments on the happening of a specified event (where there is uncertainty as to whether, or when, the event will happen), that is a fund:

(a) to which 2 or more persons contribute, and:

(i) out of which payments may be made in respect of liabilities, losses, damages or expenses of the contributors; and

(ii) that is governed by rules under which any such payment for the benefit of a contributor is subject to a discretion of a person or body; or
(b) that is declared to be a discretionary mutual fund, or included in a class of funds that are declared to be discretionary mutual funds, by regulations made for the purposes of this paragraph.

(6) However, a fund (however constituted) is not a discretionary mutual fund if:

(a) a contributor has a right, in law or equity, to a payment of a kind referred to in subparagraph (5)(a)(i); or

(b) the fund is:

(i) declared not to be a discretionary mutual fund; or

(ii) included in a class of funds that are declared not to be discretionary mutual funds; by regulations made for the purposes of this paragraph."


In plain English, DMFs are entities that offer ‘discretionary cover’, that is, an insurance-like product that may involve an obligation on the DMF to consider meeting a claim made on it, but gives the DMF a discretion as to whether it will pay the claim. DMFs may sell ‘general insurance-like’ and ‘life insurance-like’ products. A DMF may be a trust, mutual, company limited by guarantee or other structure.

DMFs typically meet directly the cost of most claims by members but they also purchase insurance to protect the DMF from large individual claims and from unexpected aggregations of claims.

Collection of data

After informal consultation, APRA has decided that collection of data will occur just once a year, rather than half yearly or quarterly, because most DMFs only produce reliable financial statements annually.

For the first collection of data for financial years ending on or between 1 January 2008 and 30 June 2008, the closing date for lodgement is four months after 30 June 2008, ie 31 October 2008.

For subsequent collections, data will be required to be submitted within four months of the end of the financial year of the DMF. This will allow DMFs sufficient time to prepare and audit the annual financial statements which will be the source of data in the financial reporting forms.

Proposed forms

APRA proposes three types of forms: a Notification Form to provide contact information to APRA, a Static Information Form to provide information on the DMF financial structure, and annual reporting forms to collect financial information each year. Informal consultations with a number of DMFs and their advisers have assisted in the development of these forms.

The annual reporting forms will collect information on income statement, balance sheet, contribution revenue, claims and insurance data. They will be submitted electronically unless special alternative arrangements are made with APRA to lodge the data on CD-ROM or in hard copy.

One-off Reporting Forms

1. Notification Form – Submitted initially when the DMF first notifies APRA of its existence. Contains the name, address and other contact information for the DMF. Also supplied on winding up for any DMF that winds up after 30 June 2008.

2. Static Information Form – Submitted initially as part of the first submission. This form collects information on the financial structure of the DMF, such as insurance arrangements and fund member entitlements and obligations. Resubmitted at any time that changes are made that cause the original form to be out of date. Resubmission to occur within two months of the changes that cause the resubmission.
Annual Reporting Forms

Assets, liabilities and equity at balance date
5. Statement of Financial Position – details of assets, liabilities and equity. For the first lodgement only, an additional Statement of Financial Position at the beginning of the financial year is also needed.

Income and expense
7. Contribution revenue by State and Territory and insurance expense – details of contributions and insurance expense by class of business.
8. Claims Expense and Insurance Recoveries - details of claims expense and insurance recoveries by class of business.

Other Information
9. Insurance – details of the DMF’s insurance cover by class of business.
10. Other information – details on the basis of accounting and audit opinion.

Proposed reporting
Forms 3 to 10 above need to be submitted annually by each DMF after the end of each financial year.
APRA seeks the views of interested parties on matters such as whether:
• the proposed forms and instructions are clear and understandable;
• there are data items in the proposed forms which are not well defined or not relevant;
• there are additional data items which should be included in the forms;
• any of the data items in the Static Information Form are likely to change from year to year;
• it is preferable to submit the Static Information Form annually rather than for the first lodgement only. This would reduce the risk to DMFs of failing to notify APRA within two months of changes to any of the information; and
• DMFs annual financial statements are, or need to be audited.
Questions and answers

Below is a series of questions and answers which provide information on APRA’s proposed reporting requirements.

1. Why is APRA collecting data?
The Government has asked APRA to collect data from DMFs so that the Government can understand the nature and scope of DMF operations and the role of DMFs in providing insurance-like products and services. Data collected will be used to assist the Government to review, within three years, the need to prudentially regulate DMFs.

2. How does an institution know it is a DMF and needs to submit forms?
A DMF is an entity that meets the legal definition in the DMF Act. A DMF that meets the definition and is in existence on or after 30 June 2008 must submit forms.

3. Are there penalties if the reporting forms are not lodged on time?
FSCODA contains provision for penalties to be applied if reporting obligations are not met. APRA’s practice, however, is not to apply penalties automatically to entities that are making a bona fide attempt to comply with their reporting obligations.

4. Is submission of the Notification Form compulsory for DMFs?
Yes, it is compulsory for DMFs that exist at 30 June 2008 or come into existence after 30 June 2008 to complete the Notification Form and return it to APRA.

5. Why does APRA want the Notification Form completed?
The Notification Form will allow APRA to gather contact details and basic data on each DMF. This will assist APRA in contacting DMFs and informing them about Direct to APRA (D2A) software for the electronic submission of the forms.

6. How will the Notification Form be made available?
The Notification Form will be electronically available from the ‘Non-Regulated Entities’ menu at www.apra.gov.au during the first quarter of 2008.

7. When does the Notification Form need to be lodged?
DMFs will need to send the Notification Form to APRA either by 30 June 2008 or, if they commence operations after that date, within 14 days of commencing operations.

DMFs that wind up after 30 June 2008 will need to submit an additional Notification Form within 14 days of wind-up.

8. What is the Static Information Form and when does it need to be submitted?
The Static Information Form collects data that does not usually change from year to year. This data includes the financial structure of the DMF, such as insurance arrangements and fund member entitlements and obligations. Resubmitted at any time that changes are made that cause the original form to be out of date. Resubmission to occur within two months of the changes that cause the resubmission.

9. What period does each reporting form cover?
Each submission will cover the financial year of the DMF. For example, a DMF that has a financial year-end of 31 October 2008 will need to submit, by 28 February 2009, data for the financial year from 1 November 2007 to 31 October 2008.

10. What level of reporting does APRA want?
DMFs will generally need to submit data at the legal entity or trust level. Some DMFs, however, operate with multiple subfunds. Where the DMF has separate subfund bank accounts and subfund financial statements, all reporting forms, except the Notification Form, will need to be submitted for each subfund.
11. What basis of accounting do DMFs use when completing the reporting forms?
DMFs should use the same basis of accounting that is used for their financial statements.

12. Does the data submitted to APRA need to be audited?
The completed APRA reporting forms do not need to be audited. However, the data should be based on the DMF’s financial statements, preferably audited, and must be subject to the same processes and controls that cover the review and authorisation of that accounting data. It is the responsibility of the board or trustee of the DMF to ensure that the information lodged with APRA is accurate and complete.

13. What does a DMF need to know about D2A software?
D2A is an application that allows organisations to download APRA forms, complete them, and send them via the internet to APRA. D2A is successfully used by APRA-regulated entities to submit forms electronically and securely.

After APRA has received a Notification Form, it will contact the DMF prior to the commencement of reporting obligations to explain how D2A software can be installed. All forms submitted to APRA using D2A are protected using cryptography (information security) in the form of a digital certificate. The digital certificate is used to digitally sign data sent to APRA, which is legally equivalent to a conventional, handwritten signature. Further detailed information on D2A is available from http://www.apra.gov.au/statistics/D2A.

14. How frequently do forms need to be submitted?
The reporting forms are annual forms and need to be lodged annually after the end of each financial year of the DMF.

15. When do DMFs need to submit the reporting forms?
For DMFs with financial year-ends falling on or between 1 January 2008 and 30 June 2008, reporting forms covering the financial year will need to be submitted to APRA by 31 October 2008.

For financial years ending after 30 June 2008, reporting forms for each financial year will need to be submitted to APRA within four months of the end of the financial year of the DMF.

16. Can APRA require DMFs to submit additional information?
Yes, additional information may be required to be lodged if APRA determines this to be necessary. It is not APRA’s intention to collect regularly any data other than what is required to complete the annual forms. Nevertheless, entities may be asked for additional information, for example the constitution of the DMF, additional financial statements or documentation of their insurance arrangements.
Submissions

APRA’s discussion paper sets out proposed data collection arrangements and invites submissions on the forms and instructions. As well as comments on the content of the Notification Form, Static Information Form and reporting forms and instructions, APRA would also appreciate commentary on any matters in the Discussion Paper which respondents would like to bring to APRA’s attention. Written submissions and queries should be emailed to DMF_Reporting@apra.gov.au for the attention of Keith Chapman, General Manager Policy Development. The closing date for submissions is Friday, 2 November 2007.