

The background features a complex geometric pattern of overlapping triangles and lines in shades of blue and purple. In the upper left corner, there is a faint line graph with a grid and numerical values (40, 50, 60) on the y-axis.

CLYDE&CO

Submission
Financial Accountability
Regime – Regulator Rules

17 August 2023

Submissions

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2 Introduction

2.1 Clyde & Co is a leading international law firm. With deep experience in financial services regulation and corporate governance, we assist domestic and global financial institutions with their most sensitive and technically complex mandates. We have extensive experience advising clients in the insurance and superannuation sectors in Australia and are therefore well placed to comment on the consultation drafts of the:

- (a) *Financial Accountability Regime Act (Information for register) Regulator Rules 2023 (Cth) (Regulator Rules)*;
- (b) ADI Key Functions descriptions, referred to as **Attachment B** in the consultation draft package (which we adopt for this submission); and
- (c) *Financial Accountability Regime (Consequential Amendments) Transitional Rules 2023 (Cth) (Transitional Rules)*,

as jointly published by APRA and ASIC in July 2023 and intended to support the implementation of the Financial Accountability Regime (**FAR**).

2.2 While the *Financial Accountability Regime Bill 2023 (Cth) (FAR Bill)* remains before the Senate as of 17 August 2023, we have prepared our submission on the assumption that the FAR Bill will be passed and become law on unchanged terms.

2.3 We have also assumed, for the purposes of preparing our submission, that the draft *Financial Accountability Regime Minister Rules 2022 (Cth) (Minister Rules)* that

were open for consultation until 7 October 2022, will become law on the same terms as were the subject of that consultation.

- 2.4 We make this submission from the perspective of, and with a particular concern for the interests of other, prudentially regulated entities which will come under the FAR remit that are not ADIs. In particular, we focus our submission (as we focus our practice) on general insurance, life insurance, private health insurance and superannuation.

3 **Summary of submissions**

- 3.1 We have summarised our submissions in relation to the Regulator Rules, in the sub-paragraphs below:

- (a) The Regulators Rules do not (and should not) expand, modify or otherwise have any legal effect on the proper interpretation of who an accountable person is for the purposes of the FAR;
- (b) The Column 2 preamble in Attachment B (describing the ADI Key Functions) should be re-drafted to clarify that the identification of a person as an accountable person in accordance with the law is paramount, and that the ADI Key Function descriptions in Attachment B are merely non-exhaustive indicia of functions within a regulated institution which may or may not be held by accountable persons;
- (c) As the operations, challenges and risks faced by ADIs on the one hand, and insurers and superannuation entities on the other, are inherently different, we submit that the ADI Key Functions set out in the table in section 6 of our submission be appropriately modified or omitted entirely from future draft key functions descriptions for insurers and RSEs;
- (d) Attachment B, as currently drafted, may cause regulated institutions to inappropriately nominate lower level managerial staff as accountable persons, and in turn, create duplicative efforts and activities to assist those persons to satisfy their reasonable steps obligations; and
- (e) The inclusion of the ADI Key Functions as described in Attachment B exacerbates a significant disconnect that regulated institutions are already grappling with in regards to the three lines of defence model.

- 3.2 We are very grateful for the time and effort that the regulators have spent on the Regulator Rules; we would be happy to participate in any further discussions or to answer any questions which may assist their further development.

4 **Key Functions – what are they trying to achieve?**

- 4.1 Pursuant to section 40(4)(g) of the FAR Bill, the Regulator Rules prescribe certain information (being, the ADI Key Functions as defined in the Regulator Rules) that must be included in the register of accountable persons. Relevantly, section 5(1) in Part 2 of the Regulator Rules provides:

For the purposes of paragraph 40(4)(g) of the Act, the following information is prescribed for inclusion in the register: ...

- (j) *key functions—each ADI Key Function (if any) of the accountable person;*

(k) the dates the accountable person assumed, and ceased to have, responsibility for each ADI Key Function referred to in paragraph 5(1) (j) (if applicable);

4.2 The new concept of an ADI Key Function is defined in section 4 of the Regulator Rules. This definition is further explained in Attachment B, although those descriptions do not form part of the Regulator Rules.

4.3 Importantly, the Regulator Rules do not expand, modify or otherwise have any legal effect on the proper interpretation of who an accountable person is for the purposes of FAR. For that, reference must be made to sections 10 and 11 of the FAR Bill, and neither of those sections contemplate that they are subject to change pursuant to the Regulator Rules. It follows that addressing any lack of clarity in those sections is a matter for Government to resolve through legislative amendment (or if appropriate, through amendment to the Minister Rules).

4.4 We note, however, that the covering letter accompanying the Regulator Rules jointly issued by APRA and ASIC on 20 July 2023 suggests that the Regulators will use the ADI Key Functions to assist the Regulators to assess whether accountabilities have been appropriately assigned. This approach does not align with the drafting of the FAR Bill and the Regulator Rules themselves. Specifically, the covering letter states that the ADI Key Functions:

“are intended to help the Regulators assess whether accountable entities are adequately assigning accountability across all operational areas to their accountable persons (i.e. key functions can only be assigned to accountable persons)”

4.5 Similarly, the Regulator Rules are not appropriate to be relied on by the Regulators to obtain information that is not otherwise within the remit of the FAR Bill to be collected. For example, if Government desired the Regulators to be informed of the same information that is provided in accountability statements and accountability maps for all accountable persons, the legislation should provide for that, not the Regulator Rules.

4.6 We are concerned that the breadth of persons potentially captured by the ADI Key Functions descriptions is far wider than the intended remit of FAR. We submit that the identification of accountable persons is a task to be undertaken by each regulated institution in accordance with the FAR Bill, the Minister Rules and Regulator Rules in the context of its unique circumstances. The Regulator Rules should not be considered by Regulators in their assessment of the appropriateness or otherwise of an institution’s determination of its accountable persons. In our view, this statement creates a significant and unnecessary uncertainty for regulated institutions under FAR which could disproportionately increase the compliance burden of the regime and distract institutions from achieving the objectives of FAR in its implementation.

5 **The Key Functions descriptions need refining**

5.1 The concept of an ADI Key Function is defined in section 4 of the Regulator Rules, and further explained in Attachment B. While the ADI Key Function descriptions in Attachment B do not form part of the Regulator Rules, the covering letter for the consultation package states: “each key function that is applicable to the ADI must be assigned to at least one accountable person and recorded in the FAR register”.

5.2 Column 2 of Attachment B contains a lengthy preamble applying to each of the ADI Key Functions. It states:

“An accountable person holds the key function in Column 1 if they have primary conduct of, or key decision-making power in relation to, the overall development, maintenance, oversight, review or execution of one or more aspects of the relevant key function as described in this Column 2”

- 5.3 This preamble combines a number of concepts, some of which are inconsistent with the intended ambit of FAR when read alongside the FAR Bill, its Explanatory Memorandum, the Minister Rules and its Explanatory Statement.
- 5.4 By virtue of the drafting of the preamble in Column 2 of Attachment B, there are a number of curious combinations which seem to us to not have been intended. For example, a person having “primary conduct of” the “execution” of one or more aspects of the ADI Key Function is analogous to a person “merely carrying out those activities or functions” which is expressly described as not being the intended focus of the Minister Rules that prescribe accountable person responsibilities for FAR purposes (see the Explanatory Statement for the Minister Rules, and for example, sections 5(3) and 7(3) of the Minister Rules).
- 5.5 We submit that the Column 2 preamble in Attachment B should be removed and replaced by text that reiterates that the identification of a person as an accountable person in accordance with the law (i.e. sections 10 and 11 of the FAR Bill) is paramount, and that the ADI Key Function descriptions in Attachment B are merely non-exhaustive indicia of functions within a regulated institution which may or may not be held by accountable persons.
- 5.6 Further, in the absence of clarifying text in the Regulator Rules or the ADI Key Function descriptions in Attachment B, we submit that confusion will potentially be caused amongst regulated entities. To mitigate this risk, we submit that the ADI Key Functions be clearly and unambiguously described as not representative of, or corresponding to, to the full range of roles and responsibilities for which accountable persons must be identified for the purposes of FAR.

6 Key Functions which won't work more broadly

- 6.1 We appreciate that the ADI Key Functions are only intended for ADIs, and that future consultations will be held to consider key functions for other APRA regulated institutions that will become subject to FAR in due course. We have nevertheless, and in accordance with the Regulators' suggestion in the covering letter to this consultation package, turned our minds to the potential extension of the ADI Key Functions to insurers and RSEs.
- 6.2 As the operations, challenges and risks faced by ADIs on the one hand, and insurers and RSEs on the other, are inherently different, we submit that the ADI Key Functions set out in the table below be appropriately modified or omitted entirely from future draft key functions descriptions for insurers and RSEs. A prevailing theme of our submissions is that the ADI Key Functions, if applied to insurers and RSEs, would be unnecessarily duplicative of existing concepts and requirements of FAR.
- 6.3 We note further that the ADI Key Functions seem to reflect a relatively narrow focus on compliance with specific financial services regulatory obligations, rather than on a more holistic, organisation-wide level, view of resilience.

ADI Key Function	Submission	Comments
Collections and enforcement (default, debt collections, and recovery)	Remove	<p>This is not a key function for insurers in respect of dealings with policyholders given the strict regulation of the powers and rights of insurers arising in the event of non-payment of premium.</p> <p>Similarly, this is not a key function for RSEs in respect of dealings with members given the strict regulation of the use of member contributions.</p>
Credit risk management	Remove	<p>As above in respect of dealings with policyholders for insurers, and in respect of dealings with members for RSEs. And insofar as this concerns other dealings, this area is adequately captured by the following prescribed responsibilities under the Minister Rules:</p> <ul style="list-style-type: none"> • senior executive responsibility for management or control of the accountable entity's financial resources; • senior executive responsibility for management of the accountable entity's overall risk controls or overall risk management arrangements; and • for RSEs, senior executive responsibility for management of the accountable entity's investment function.
Data management	Remove	<p>This area is adequately captured by the general definition in section 10(1) of the FAR Bill. If, and to the extent, that it is not so captured for a particular insurer or RSE, it will be by virtue of the Minister Rules prescribed senior executive responsibility for management of the accountable entity's information management (including information technology systems).</p>
Financial and regulatory reporting	Remove	<p>This area is adequately captured by the general definition in section 10(1) of the FAR Bill. If, and to the extent, that it is not so captured for a particular insurer or RSE, it will be by virtue of the following prescribed responsibilities under the Minister Rules:</p> <ul style="list-style-type: none"> • senior executive responsibility for management or control of the accountable entity's financial resources; and • senior executive responsibility for management of the accountable entity's compliance function.

ADI Key Function	Submission	Comments
Financial services regulatory engagement	Remove	This is not a key function, but rather, is a key accountability obligation imposed on all accountable persons under section 21 of the FAR Bill (and on accountable entities under section 20 of the FAR Bill).
Liquidity and funding management	Remove	<p>This area is adequately captured by the following prescribed responsibilities under the Minister Rules:</p> <ul style="list-style-type: none"> • senior executive responsibility for management or control of the accountable entity’s financial resources; • senior executive responsibility for management of the accountable entity’s overall risk controls or overall risk management arrangements; • for insurers, senior executive responsibility for management of the accountable entity’s actuarial function; and • for RSEs, senior executive responsibility for management of the accountable entity’s investment function.
Market risk management	Remove	<p>This area is adequately captured by the following prescribed responsibilities under the Minister Rules:</p> <ul style="list-style-type: none"> • senior executive responsibility for management or control of the accountable entity’s financial resources; • senior executive responsibility for management of the accountable entity’s overall risk controls or overall risk management arrangements; and • for RSEs, senior executive responsibility for management of the accountable entity’s investment function.
Product design and distribution obligations	Remove	The product design and distributions obligations regime necessarily involves a range of key functions and responsibilities, all of which are adequately captured by either the general definition in section 10(1) of the FAR Bill and/or the prescribed responsibilities in the Minister Rules. Further, we note that it is for these same reasons that the previously proposed senior executive responsibility for “end-to-end product” has been removed from the Minister Rules.

ADI Key Function	Submission	Comments
Risk culture	Remove	This area is adequately captured by the Minister Rules prescribed senior executive responsibility for management of the accountable entity's overall risk controls or overall risk management arrangements.
Scam management	Remove	<p>This is not a key function within an insurer or RSE.</p> <p>Insofar as insurers' practices designed to prevent consumer loss from fraudulent activity (e.g. in the context of claims), this is a function that is adequately captured by the Minister Rules prescribed senior executive responsibility for management of the accountable entity's claims handling function.</p> <p>Similarly, insofar as RSEs practices designed to prevent member loss from fraudulent activity (e.g. in the context of early withdrawals or insurance claims), this is a function that is adequately captured by the Minister Rules prescribed:</p> <ul style="list-style-type: none"> senior executive responsibility for management of the accountable entity's member administration operations; and senior executive responsibility for management of the accountable entity's insurance offerings.
Technology management	Remove	This area is adequately captured by the Minister Rules prescribed senior executive responsibility for management of the accountable entity's information management (including information technology systems).

7 Reasonable steps

- 7.1 We submit that the ADI Key Functions descriptions in Attachment B extend too far and too deep into managerial and operation responsibilities which fall outside the intended ambit of FAR. In the FAR Bill, the Government has made its intention clear that accountable persons should only be the most senior executives who are appropriately accountable for their relevant roles and responsibilities within a regulated institution.
- 7.2 While we appreciate that the Regulator Rules do not intend to, and cannot, expand the operation of FAR, we submit that the inclusion of the ADI Key Functions descriptions in Attachment B, as currently drafted, may cause regulated institutions to inappropriately nominate lower level managerial staff as accountable persons, and in turn, create duplicative efforts and activities in an effort to assist those persons to satisfy their reasonable steps obligations. To

illustrate the complexity of this, we include as **Annexure 1** an illustrative example of the core elements of a control map for each accountable person.

7.3 Annexure 1 to our submission also serves a secondary purpose in illustrating the some of the “reasonable steps” considerations that organisations may need to have in place for their accountable persons who are taking on personal liability for the responsibilities set out in their accountability statements. Without a consideration of such matters, which tie into the legislation requirements under section 22 of the FAR Bill, executives may consider themselves exposed if and when APRA and ASIC query how a stated responsibility is discharged from a “reasonable steps” perspective.

7.4 In preparing Annexure 1, we have also had reference to the UK FCA Handbook for the Senior Manager’s Certification Regime, including CONCON 4.2.6 which requires that Senior Managers:

“... should take reasonable steps to satisfy themselves, on reasonable grounds, that each area of the business for which they are responsible has appropriate policies and procedures for reviewing the competence, knowledge, skills and performance of each individual member of staff.”

8 Blurring of the three lines of defence model

8.1 Finally, we submit that the inclusion of the ADI Key Functions as described in Attachment B exacerbates a significant disconnect that regulated institutions are already grappling with in regards to the three lines of defence model.

8.2 The three lines of defence model is utilised by most, if not all, APRA-regulated institutions, and generally ascribes risk owners (i.e. operational staff and management) as the first line of defence, the Risk and Compliance functions as the second line of defence, and Internal Audit as the third line of defence. A fundamental tenet of this globally recognised risk management model is the independence of the second (and third) lines from the first. We submit that the inclusion of roles and responsibilities in the ADI Key Functions which are typically occupied by personnel in the second line of defence is inconsistent with the model and may undermine their independence.

8.3 In our view, and tying into the three lines of defence consideration, there is also insufficient attention drawn to the fact that one area will involve multiple accountable persons each performing different roles.

8.4 For example, data management is described in Attachment B as follows:

“Data management including data strategy, data architecture, data management framework and governance, data quality and issue management, data risk management including the state of data controls and data privacy”.

Should the Chief Technology Officer (**CTO**) be responsible for specific data quality which is poor, where the data has been collected by the marketing team that stepped outside of the data management policy / framework excellently prepared by the CTO? Likewise, should the Chief People Officer be held accountable for breaches of the bullying and harassment policy and framework which was good in construction, but not followed or acted on by, say, the CTO’s team? Some aspects, like data management and HR issues, have the boundaries manufactured by a particular specialist area, however, are the whole organisation’s issue to get right. Data management and bullying and harassment are but two examples.

- 8.5 In essence, there should be an acknowledgement of the functional role of each director and executive. As a rule of thumb, in our experience, there are usually five roles for each area of risk or responsibility, being:
- (a) decision makers (usually Board / CEO);
 - (b) manufacturers (e.g. of a policy);
 - (c) implementers (e.g. of a policy from another division);
 - (d) overseers (e.g. of a particular process); and
 - (e) leaders (e.g. of a division).

All accountable persons will have a combination of these functional roles. For instance, no accountable person will just be an “implementer”. They may, and very likely, will also have accountabilities of a “leader”, “manufacturer” and “overseer”. Having consistent and understood definitions reduces director and executive risk when ASIC and APRA are interpreting an accountability statement from an enforcement perspective.

- 8.6 To the extent it is helpful, we have set out these functionally separate areas in **Annexure 2** for consideration. We think that the functional areas need to draw out these differences to a greater extent to assist the regulated population, lest generality lead to unintended and unfair risk to individuals.

We would be pleased to discuss our submission. Please feel free to contact any of the authors at your convenience.



[REDACTED]
Partner
[REDACTED]



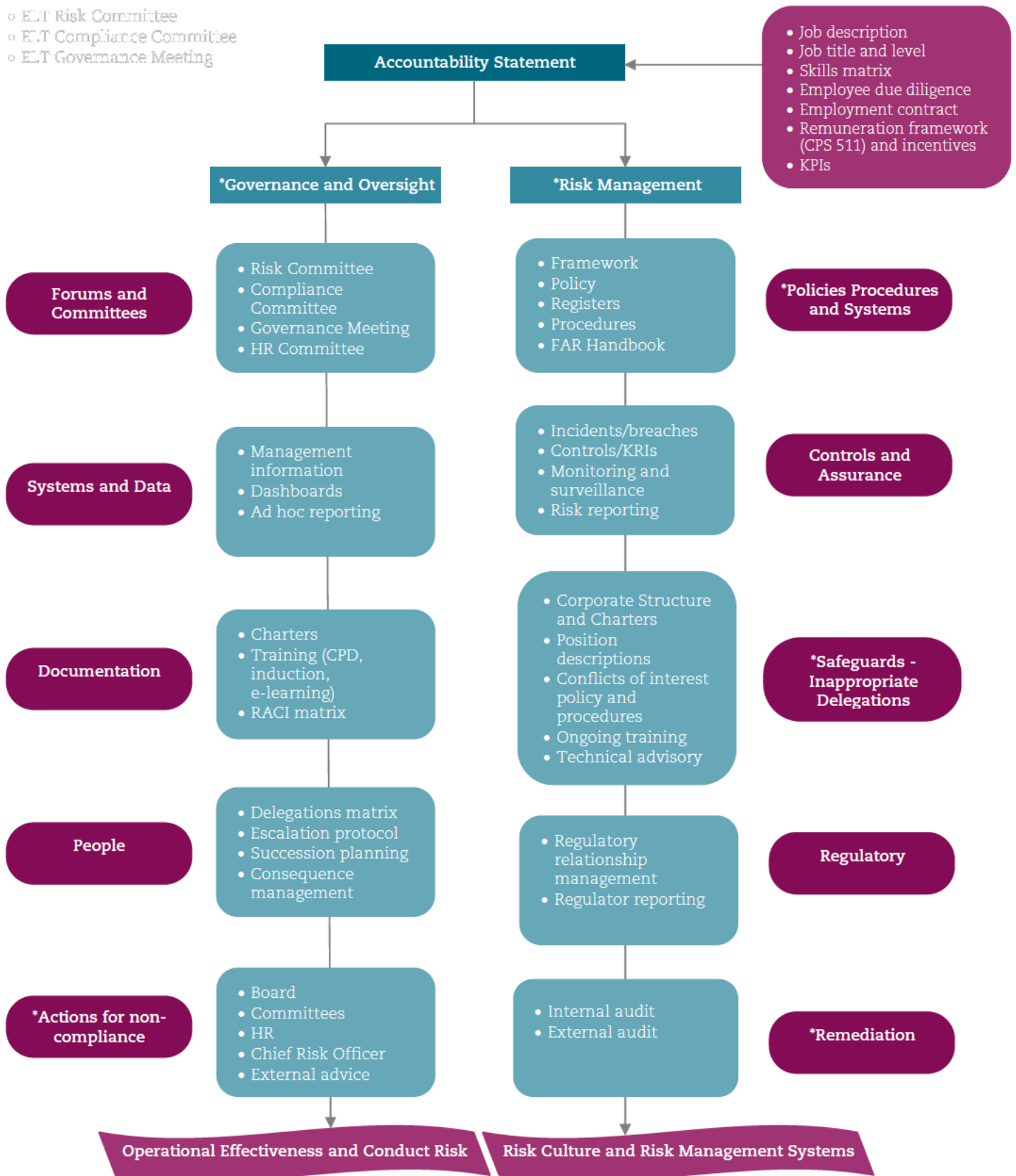
[REDACTED]
Partner
[REDACTED]



[REDACTED]
Partner
[REDACTED]

Annexure 1 – Desktop reasonable steps considerations

- o ELT Risk Committee
- o ELT Compliance Committee
- o ELT Governance Meeting



* Indicates that these factors are required and specifically set out under section 22 of the FAR Bill.

Annexure 2 – Verb Glossary

Category	Accountability statement verbs			
<p>Making decisions</p> <p>The process of making decisions (or the application or decision-making techniques).</p>	Advising	Approving	Identifying	Consulting
	Reviewing	Negotiating	Performing	Decision making
	Confirming	Responding	Executing	Making
	Providing	Assessing	Acting	Determining
	Escalating	Planning	Writing	Addressing
	Appointing	Setting	Giving	
<p>Manufacturing</p> <p>The process of producing something, or bringing something into existence.</p>	Developing	Reporting	Scoping	Designing
	Creating	Preparing	Assisting	Collating
	Formulating	Producing	Conducting	Soliciting
	Establishing	Receiving	Contributing	
	Collecting	Proposing	Gathering	
	Coordinating	Defining	Obtaining	
<p>Implementing</p> <p>The process of putting something into action or practice.</p>	Recommending	Undertaking	Adopting	Collaborating
	Delivering	Administering	Applying	Facilitating
	Embedding	Working	Managing	Submitting
	Enforcing	Improving	Expanding	Progressing
	Implementing	Complying	Enhancing	
<p>Overseeing</p> <p>The process of supervising someone or something.</p>	Monitoring	Analysing	Challenging	Supporting
	Ensuring	Protecting	Interpreting	Considering
	Supervising	Understanding	Evaluating	
	Maintaining	Endorsing	Engaging	
	Overseeing	Questioning	Refining	
<p>Leading</p> <p>The process of guiding a company toward its goals and objectives.</p>	Demonstrating	Promoting	Advocating	Growing
	Representing	Leading	Driving	Embodying
	Communicating	Achieving	Guiding	Educating

490

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