



5 October 2011

To chief executive officers of Level 2 insurance groups

Finalisation of refinements to the prudential framework for Level 2 insurance groups

In May 2011, APRA released a consultation package comprising a discussion paper, three draft prudential standards and a suite of draft reporting forms and instructions.¹ This package proposed a number of refinements to the prudential and reporting framework for Level 2 insurance groups. The package proposed to align aspects of the reporting framework for Level 2 insurance groups and individual APRA-authorized general insurers.

APRA received four submissions on the consultation package. The submissions broadly supported APRA's proposals. Submissions endorsed APRA's proposed refinements, welcoming the alignment of the reporting frameworks and noting that the refinements struck an appropriate balance between benefits and additional obligations. The submissions sought clarification on a number of the proposals.

Following consideration of the submissions, APRA has released three prudential standards and eight reporting standards applicable to Level 2 insurance groups. All of the standards are available on APRA's website.² The reporting forms are expected to be available in D2A from late 2011.

APRA has also provided, as reference, versions of all of the prudential standards, as well as forms and instructions, marked up to indicate the changes that have been made.

The prudential standards are effective on 1 December 2011 and the reporting standards are effective for reporting periods commencing on or after 1 July 2011. The first half-yearly reporting on the revised basis will be for the period ending 31 December 2011 and is due on 31 March 2012.

The policy position in the final prudential and reporting standards is largely consistent to APRA's proposals in the discussion paper. APRA has implemented the refinements to the definition of a Level 2 insurance group, actuarial matters, intra-group exposures and remuneration schemes. APRA has amended its approach to governing law requirements and this is outlined further below. APRA has also implemented the refinements to the reporting framework, with the exception of one small revision and one clarification which are also outlined below.

¹ Consultation package: <http://www.apra.gov.au/Policy/Pages/Refinements-to-the-prudential-framework-for-general-insurance-groups-May-2011.aspx>

² Final package: <http://www.apra.gov.au/GI/PrudentialFramework/Pages/Refinements-to-the-prudential-framework-for-general-insurance-groups-October-2011.aspx>

Amended Proposals

In response to submissions received, APRA has made revisions to two of the original proposals in the final prudential and reporting standards:

Reinsurance arrangements and governing law requirements

In the discussion paper, APRA proposed to require deduction from capital of the Level 2 insurance group any reinsurance assets which do not meet relevant governing law requirements in a foreign jurisdiction and are required to be deducted from capital in that jurisdiction.

Submissions raised a number of concerns with this requirement: differences in prudential frameworks around the world, including frequency of reporting, makes this difficult to implement; unintended impacts and consequences for reinsurance which covers more than one jurisdiction; and the possibility of decreased legal effect of reinsurance contracts which have additional jurisdiction clauses. Submissions requested that APRA apply a more flexible approach to the implementation of this requirement.

APRA has considered the feedback received and has revised its approach to governing law requirements in foreign jurisdictions. The capital standards no longer require reinsurance assets not meeting governing law requirements in foreign jurisdictions to be deducted. However, APRA expects that Level 2 insurance groups understand and comply with relevant regulatory requirements in jurisdictions in which they operate. APRA will continue to review foreign reinsurance assets, including their eligibility in foreign jurisdictions, as part of normal supervisory processes. APRA may consider the application of a supervisory adjustment if it is concerned about the management or recoverability of foreign reinsurance assets.

Assets with a counterparty grade 1 or 2

In the discussion paper, APRA proposed to introduce additional line items on *Reporting Form GRF 300.0_G Statement of Financial Position (Level 2 Insurance Group)* (GRF 300.0_G) to ensure that the correct risk charge from *GPS 114 Capital Adequacy: Investment Risk Capital Charge* as read with *GPS 111 Capital Adequacy: Level 2 Insurance Groups* is applied to assets with a counterparty grade 1 or 2 with varying maturities.

Submissions noted that the collection and consolidation of the information would be a significant task which would be both onerous and immaterial from a capital requirement perspective.

APRA has accepted the concerns raised by respondents in their submissions. APRA also notes that the differing risk charges will no longer be applicable when the current insurance capital review project is completed in 2013. Therefore, the proposed additional reporting of maturity information to calculate the differing risk charges on GRF 300.0_G will not be implemented.

Clarifications

APRA provides the following clarifications and additional information in relation to the operation of two proposals:

Actuarial peer review and intra-group transactions

Submissions sought further clarification on the application of additional powers introduced in the prudential standards with respect to actuarial peer review and intra-group exposures.

The additional powers assist APRA in its objective of ensuring Level 2 insurance groups are financially sound and that the financial and operational interrelationships within the group do not compromise the financial position of any APRA-authorized members of the group. APRA would use these powers in circumstances where APRA is of the view that to do so would provide

APRA with additional and beneficial information to achieve its objectives. As part of normal supervisory processes, discretion will be applied by the Responsible Supervisor of the Level 2 insurance group with regards to the appropriateness, materiality and application of these powers.

Risk charge for 'current tax assets' on the statement of financial position

In the draft reporting form for the statement of financial position (GRF 300.0_G), APRA proposed to separate 'current tax assets' from 'other assets' to align the reporting of tax items with the reporting requirements for individual insurers. The draft reporting form inadvertently omitted the risk charge for current tax assets. This has been amended in the final reporting standard, form and instructions.

A number of other comments were received regarding the alignment of the reporting frameworks for individual insurers and Level 2 insurance groups. APRA has considered the issues raised and has determined that it is appropriate to implement the alignment of the two frameworks as outlined in the discussion paper.

Transition arrangements

The final prudential standards include provisions which preserve the operation of all determinations made under previous versions of the standards. Accordingly, Level 2 insurance groups are not required to re-apply to APRA to ensure the continuation of such determinations.

Level 2 insurance groups that may be unable to meet these amended prudential requirements by the due date should contact their Responsible Supervisor at the earliest opportunity. APRA considers that absent compelling circumstances, all insurance groups should be able to meet these requirements by 1 December 2011 and report accurately upon them by the March 2012 due date.

For further information please contact Kate Bible (02 9210 3502) or email GILevel2@apra.gov.au.

Yours sincerely



Helen Rowell
General Manager - Policy Development