The BEAR: a radical structural shift for insurers?

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AT A GLANCE

Executive accountability for financial product design, promotion, delivery and remediation was a major theme in the Final Report of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry. It is an issue which insurers will need to grapple with if one of the less publicised, but potentially very significant, recommendations in the Final Report becomes law.

THE PROBLEM

A key issue seized upon by Commissioner Hayne in exploring how misconduct became institutionalised within certain organisations was the lack of 'cradle to grave' or 'life cycle' oversight of product design, promotion, delivery and remediation.

In exploring this issue, Commissioner Hayne highlighted the observations of ANZ's CEO, Shayne Elliott, that there is no-one 'accountable from the design of the product through to its implementation and if something goes wrong, remediating it and, importantly, keeping it fit for purpose".

This perceived gross deficiency in product management and executive accountability gave rise to Commissioner Hayne's recommendation that the **"Banking Executive Accountability Regime"** (**BEAR**) be extended in scope and applied to insurers. It is a recommendation which could have far-reaching structural and operational implications for insurers.

WHAT IS THE BEAR?

The BEAR currently forms part of the *Banking Act 1959* (Cth) and imposes a series of obligations on banks and their "accountable persons" regarding their conduct.

Some notable aspects of the BEAR are that:

- it requires banks and their accountable persons to take reasonable steps to conduct their business with honesty, integrity, due skill, care and diligence and prevent matters from arising that would adversely affect the bank's prudential standing or prudential reputation
- it requires that accountable persons be in a senior executive or board member position, and must apply and be approved for entry on APRA's register of accountable persons
- banks are prohibited from indemnifying or taking out insurance for breaches of an accountable person's obligations
- there must be mechanisms in place to defer, and if necessary, reduce the variable remuneration[1] payable to an accountable person if they fail to comply with their accountability obligations
- a bank's notification obligations require it to provide APRA with accountability statements and accountability maps. Accountability statements are required to set out the aspects of the bank's operations for which the accountable person has control (including the nature of the responsibilities held by that person). Accountability maps must set out all of the accountable persons and their reporting lines. Banks are required to notify APRA when, among other things, the variable remuneration of a person has been reduced, and when breaches of the accountability obligations of due care and skill have occurred, and
- non-compliance with the BEAR has regulatory ramifications, including the imposition of pecuniary penalties on banks.

[1] Partly defined as "*so much of the accountable person's total remuneration as is conditional on the achievement of objectives…*"

AMENDMENTS TO THE BEAR

Commissioner Hayne has recommended that:

- the BEAR be expanded to include express responsibilities for steps in the "design, delivery and maintenance of all products offered to customers…and any necessary remediation of customers in respect of any of those products" (recommendation 1.17)
- provisions modelled on the BEAR should be extended to all APRA-regulated insurers (recommendation 4.12) and, over time, to all APRA-regulated financial services institutions (recommendation 6.8), and
- ASIC and APRA should jointly administer the BEAR, with consequential amendments made to the relevant legislation (recommendations 6.6 and 6.7).

These recommendations, if implemented, will mean that an expanded version of the BEAR which, most importantly, includes extending the accountable person model to the life cycle of a product, will apply to insurers

IMPLICATIONS FOR INSURERS

It is highly likely that the recommendations made by Commissioner Hayne regarding the BEAR will be implemented, given Treasury's agreement with those recommendations[2] – although its consultation process has not yet commenced.

Fundamentally, the recommended extension of the BEAR, along with its application to the conduct of insurers, is likely to require a single, senior officer to act as an accountable person for a product, or suite of products, throughout its life cycle.

This means that, from an accountability regime perspective, the accountable person will be responsible for the compliance of product design, promotion, delivery and, if required, customer remediation in a manner consistent with the principles of the BEAR.

[2] Treasury, 'Restoring trust in Australia's financial system: The Government response to the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry' (February 2019).

In addition, accountable persons will have any performance driven component of their remuneration deferred and linked to compliance outcomes.

While, at a general level, 'personal' responsibility already rests with officers of an insurer for the conduct of the organisation, the application of the BEAR to insurers in the manner recommended by Commissioner Hayne represents a significant amplification of that personal duty.

At a minimum, an insurer will need to identify accountable persons within its senior ranks who will be personally responsible for a product across its life cycle, document its accountability plans and processes, and implement them.

It seems inevitable that this will require some level of organisational change for insurers.

A NEW APPROACH TO PRODUCT LIFE CYCLE

Responsibility allocated across traditional disciplines of underwriting, actuarial, compliance, claims and legal will need to be supplemented by a structure which implements an accountable person approach to a product across its life cycle. For some insurers, this could represent a radical shift in the way they are structured with divisional, vertical responsibility lines being supplemented by a horizontal, accountable person model directed at oversight of products during their life cycle.

It also 'ups the ante' for those in senior positions who assume personal responsibilities, as compliance failings will give rise to both personal and organisational exposure. It is clearly anticipated by Commissioner Hayne that personal accountability for products across their life cycle ought to ensure that the conduct highlighted in the Royal Commission will not arise again or, at least, be identified and addressed far earlier, as individuals will be driven by their personal responsibilities and remuneration to ensure compliance with the law.

Need to know more?

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