

Life Insurance Amendment Regulations 1999 (No. 1) 1999 No. 146

EXPLANATORY STATEMENT

Statutory Rules 1999 No. 146

Issued by the Authority of the Minister for Financial Services and Regulation

Life Insurance Act 1995

Life Insurance Amendment Regulations 1999 (No. 1)

Section 253 of the *Life Insurance Act 1995* (the Life Insurance Act) empowers the Governor-General to make regulations:

- (a) prescribing matters required or permitted by this Act to be prescribed, other than matters required or permitted to be prescribed by Prudential Rules or actuarial standards; or
- (b) prescribing matters necessary or convenient to be prescribed for carrying out or giving effect to this Act.

Section 162C of the Life Insurance Act provides that regulations may set out modifications of the Act that are to apply to friendly societies (other than modifications to a provision of the Act that creates an offence, or to include new provisions that create an offence).

The purpose of the regulations is to amend the *Life Insurance Regulations 1995* (the principal Regulations) as a consequence of amendments to the Life Insurance Act resulting from the *Financial Sector Reform (Amendments and Transitional Provisions) Act (No. 1) 1999* (FSR Act) which received Royal assent on 17 June 1999. The amendments are part of the second stage of legislative reforms to implement the Government's response to the recommendations of the Financial System Inquiry as announced by the Treasurer, the Hon. Peter Costello, M.P., in the House of Representatives on 2 September 1997. The second stage of the reforms involves transferring State-based financial institutions i.e. building societies, credit unions and friendly societies (those offering financial products to members through benefit funds), to the Commonwealth regulatory regime.

The regulations will serve the following objectives:

- * to make minor modifications to the principal Regulations for life insurance companies in a manner consistent with the amendments to the Life Insurance Act that were provided for in Schedule 4 of the FSR Act which commences on 1 July 1999;
- some modifications update the principal Regulations to make them consistent with Corporations Law concepts that were introduced by the *Company Law Review Act 1998*;
- * to modify the application of the Life Insurance Act and the principal Regulations for those friendly societies that are to be prudentially regulated as life insurance companies. The modifications deal with certain structural and operational differences between friendly societies and other life insurance companies;
- parts of the regulations will serve a transitional role as friendly societies are still adjusting to the requirements of the Friendly Societies Code (which in most **States and Territories** commenced on 1 October 1997);

- most of these modifications will be contained in a proposed new Schedule 5 of the principal Regulations.

- * to further modify the application of the Life Insurance Act in its application to jointly regulated friendly societies, ie those friendly societies that operate both life insurance business and health insurance business and will thus be regulated under both the amended Life Insurance Act and the National Health Act.

- most of these modifications will be contained in a proposed new Schedule 6 of the Life Insurance Regulations. The primary purpose of Schedule 6 is to establish a process for the Australian Prudential Regulation Authority (APRA) to regulate the life insurance business of a jointly regulated friendly society under the Life Insurance Act and the Minister for Health and Aged Care and/or the Private Health Insurance Advisory Council (PHIAC) to regulate its health insurance business under the National Health Act. In cases where regulatory action needs to proceed over both types of insurance business, or the entire society, this regulation will enable certain provisions of the Life Insurance Act to also be applied to the health insurance and, other business of the society with the agreement of the Minister for Health and Aged Care or PHIAC.

- Schedule 6 will modify the application of the Act in respect to provisions that enable monitoring, investigation, judicial management, winding-up, transferring regulated business, issuing prudential standards and issuing directions to jointly regulated friendly societies.

Details of the regulations are in Attachment A.

The amendments commenced on the commencement of Schedule 4 to FSR Act. Schedule 4 commences on the ***transfer date***, which is the date specified as the transfer date for the purposes of that Act.

ATTACHMENT A

Regulation 1 - Name of regulations

The regulations are the *Life Insurance Amendment Regulations 1999* (No. 1). These regulations amend the *Life Insurance Regulations 1995* (the principal Regulations).

Regulation 2 - Commencement

These regulations commenced on the commencement of Schedule 4 to the *Financial Sector Reform (Amendments and Transitional Provisions) Act (No. 1) 1999*.

Regulation 3 - Amendment of Life Insurance Regulations

The Life Insurance Regulations are amended by Schedule 1 of the Life Insurance Amendment Regulations 1999 (No. 1).

Item 1 - Name of Regulations

This Item provides a substitute for Regulation 1.01 of the principal Regulations. Regulation 1.01 will name those regulations the Life Insurance Regulations.

Item 2 - Regulation 1.03

This Item substitutes Regulation 1.03 to provide new definitions of terms that are to be used in the principal Regulations.

Item 3 - Part 2A

This Item inserts after Part 2 a new Part 2A that provides special provisions relating to life companies that are friendly societies. There are three regulations within Part 2A:

Regulation 2A.01 - Modifications of the Act in its application to friendly societies

The Act is modified in its application to friendly societies (including jointly regulated friendly societies) as set out in Schedule 5 of the principal Regulations and are further modified in its application to jointly regulated friendly societies as set out in Schedule 6 of the principal Regulations.

Regulation 2A.02 - Modifications of Schedule 1, Part A, item 6

Schedule 1 of the Life Insurance Regulations provides details of the information that is to be provided in an application for registration. Schedule 1, Part A, item 6 requires the applicant to specify particulars of the financing of proposed new life business for the greater of the period of the financing arrangements or 10 years. Regulation 2A.02 modifies the requirement in subparagraph 6(b)(ii) for an application for registration as a society under the Friendly Societies Code that is not determined before the transfer date. For such applications, the regulation has the effect of maintaining the Code's requirement for a 3 year projection of the financing arrangements.

Regulation 2A.03 - Modifications of Schedule 1, Part A, item 6

For applications for registration made after the transfer date, the proposed regulation will modify Item 6 so that the information provided about financing arrangements can be for an alternative

period, approved in writing by APRA. This provides APRA some flexibility to consider the requirements imposed on a new applicant that seeks to be a friendly society, given that the requirements under the Friendly Societies Code are for a shorter projection period, ie 3 years.

Item 4 - Regulation 4 of the Life Insurance Regulations

Regulation 4.00 relates to the notice of the establishment of a new statutory fund in conjunction with the requirements of section 33 of the Life Insurance Act. Part 2A of the Act provides a detailed process for friendly societies to establish new benefit funds that requires APRA to approve the benefit fund rules if the specified requirements are satisfied. As APRA is to be involved in the approval of benefit fund rules it does not require a separate notification of the establishment of a new benefit fund. Accordingly, Item 4 provides, in proposed 4.00(3), that Regulation 4.00 does not apply to a life company that is a friendly society.

Item 5 - Charges over the assets of approved benefit funds

Section 161 of the Life Insurance Act provides that a friendly society cannot mortgage or charge an asset of an approved benefit fund unless the approved benefit fund rules so provide. Regulation 4.00B provides an additional requirement that the assets of an approved benefit fund may be mortgaged or charged if that application is made for the advantage of the fund. This additional requirement is consistent with the requirement of section 102(2) of the Friendly Societies Code.

Subregulation 4.0013(3) does not apply this additional test to a charge in relation to a derivatives contract that satisfies the requirements of section 161 and subregulation 4.00A(l).

Item 6 - Regulation 4.02

Section 52 of the Life Insurance Act requires a life company to give APRA written notice of the division of a statutory fund and Regulation 4.02 sets out the matters and the documents required in the notice. Amendments to the Life Insurance Act which commence on 1 July 1999 replace Division 3 of Part 4 of the Act (including section 52) with provisions dealing with the restructure and termination of a statutory fund. Given the amendment of the Act, and the development of new Prudential Rules to govern the restructure and termination of statutory funds, Regulation 4.02 is no longer necessary. For this reason, Item 6 omits Regulation 4.02.

Item 7 - Regulation 9.01

Regulation 9.01 sets out the procedure to be followed before seeking Court endorsement of a scheme to transfer or amalgamate life insurance business. This Item modifies Regulation 9.01 as it applies to jointly regulated friendly societies because health insurance business have become subject to Part 9 (see Items 39 -44 of Schedule 6). The modification ensures that, where relevant, copies of any scheme or actuarial report are given to the Minister for Health and Aged Care or PHIAC prior to publishing a notice of intention to apply for Court endorsement of any scheme.

Item 8 - Regulation 9.02

Regulation 9.02 sets out the procedure and coverage for publishing a notice of intention to apply for confirmation of a scheme to transfer or amalgamate life insurance business. Item 8 modifies Regulation 9.02 in respect of jointly regulated friendly societies by broadening the definition of **affected policy owner** for the purposes of the regulation. The effect is to extend the publication requirements recognising that for jointly regulated friendly societies, there may be at least two types of policy owners affected by a scheme i.e. those owners of policies referable to a health benefits fund and those referable to approved benefits funds.

Item 9 - Regulation 10.01

This Item modifies Regulation 10.01 (that provides a prescribed form for the assignment of a life policy) so that it does not apply to a policy that is issued by a friendly society. The reason for this modification is that Section 16ZA of the Act deals with the assignment of an interest in a benefit fund issued by a friendly society and the assignment is to be undertaken in accordance with the approved benefit fund rules, rather than a prescribed form.

Item 10 -New Regulation 10. 03

This Item creates a new Regulation 10.03 that provides that Division 4 of Part 10 of the Act (that governs surrender values, paid-up policies and non-forfeiture of policies) does not apply to policies issued by friendly societies. These provisions of the Act are not relevant to friendly societies as the approved benefit fund rules of the society may deal with these matters. For example, the treatment of benefits upon surrender is specific to the approved benefit fund rules and varies between benefit fund products.

Item 11 - Regulation 13.01

The Item repeals Regulation 13.01, which provides additional detail to the dictionary definition of *eligible assets*. The dictionary definition of *eligible assets* was repealed as part of the amendments of the Life Insurance Act that commence on 1 July 1999.

Item 12 - Schedule 1, Part B, paragraph (a)

The Item replaces outdated Corporations Law concepts. This amendment is consequential on the *Company Law Review Act 1998* that replaced the concepts of the company memorandum and articles of association with the concept of a company constitution.

Items 14 and 15 will make similar modifications.

Item 13 - Schedule 1, Part B, paragraph (j)

Schedule 1, Part B, paragraph G) provides examples of promotional material to be provided with an application for registration. As friendly societies operate by way of benefit fund structures, they do not prepare all the material described in paragraph G). The Item modifies the requirement so that a company that proposes to operate as a friendly society is required to provide documents that are more relevant to its proposed operations i.e. proposed benefit fund rules and disclosure documents.

Item 16 - New Schedule 5

This Item inserts after Schedule 4 a new Schedule 5 of the Life Insurance Regulations to provide modifications of the Act in relation to friendly societies (in accordance with proposed Regulation 2A.01).

As several of the modifications serve similar purposes with respect to related provisions of the Act the following explanation is **grouped by topic**.

Treatment of Policies

Section 35 of the Life Insurance Act outlines the requirements for policy documents including the need for the statutory fund to be identified in the policy document. Friendly societies do not issue a policy document to members as the benefit fund product (or policy) is described in the benefit fund rules, as amended from time to time. That is, a common set of benefit fund rules forms the basis of the contract between all members of that fund and the friendly society. Therefore the

Life Insurance Act concept of a policy document is not relevant to friendly societies. As there are no policy documents for friendly societies it is not possible for the document to be endorsed as required by certain provisions of the Act.

The regulations reflect this difference by modifying the following provisions of the Life Insurance Act for friendly societies:

- * subsection 35(1) is omitted because the benefit fund rules establish the benefit fund product; *Item 3 of Schedule 5;*
- * subsection 35(2) is modified so that approved benefit fund rules do not make provisions that are inconsistent with section 31 of the Act; *Item 4 of Schedule 5;*
- * subsections 35(3), (4) and (5) is omitted as they deal with provisions in a policy document; *Item 5 of Schedule 5;*
- * paragraph 36(b) is omitted because the circumstances described are not applicable to a benefit fund product; *Item 6 of Schedule 5;*
- * in subsection 198(1) the reference to "policy document" is omitted; *Item 24 of Schedule 5;*
- * in paragraph 201 (1)(b) the reference to "endorsed on the policy" is omitted; *Item 25 of Schedule 5;*
- * in subsections 213(2) and 213(3) the requirement that the policy be endorsed is changed to a requirement that the approved benefit fund rules be followed to register the applicant as the owner of the policy in the circumstances set out in section 213 - *Items 26 and 27 of Schedule 5;*
- * Part 10, Division 7 is omitted because it deals with lost or destroyed policy documents; *Item 28 of Schedule 5;* and
- * subsection 229(2) is omitted as its deals with a policy document; *Item 31 of Schedule 5.*

Participating Policies and the Distribution of Surplus

Section 15 of the Life Insurance Act defines participating and non-participating benefits. The effect of the provision is that all policies issued by life companies are either participating or non-participating benefits:

- * a non-participating benefit is a benefit that does not include any entitlement to share in any distribution of profit, i.e. the return to the policy owner is specified in the policy; and
- * a participating benefit is any other benefit.

The concepts of participating and non-participating policies flow through to the Act's requirements for the allocation of profits and losses and capital payments (Division 5 of Part 4) and the distribution of retained profits and shareholders' capital (Division 6 of Part 4). The effect of the requirements is that life insurance companies must allocate all operating profit and loss of a category of a statutory fund for a period.

These concepts cannot be applied in the context of benefit funds provided by friendly societies. Rather, benefit fund products are classified as either 'defined contribution' or 'defined benefit' funds. That is:

* In defined contribution funds, the benefit is a function of the contributions made by the member and the investment performance of the funds (eg declared bonuses). These funds could not be classed as participating in terms of section 15 of the Act because the society may exercise discretion as to what portion of the generated surplus is to be distributed to members and what portion is to remain unallocated.

* In defined benefit funds, the amount of the benefit is specified in the benefit fund rules. The benefit.

The Friendly Societies Code provides more flexibility for the friendly society to decide how much of the surplus is distributed in any period. In particular, it is not necessary for the friendly society to distribute all surplus within the period.

As a result of these differences the regulations disapply these provisions of the Life Insurance Act and reapply the approach used in section 108 of the Friendly Societies Code. In particular, the following modifications to the application of the Life Insurance Act to friendly societies are set out in the regulations:

* Section 15 dealing with the concepts of participating and non-participating benefits is disappplied; Item 1 *of Schedule 5*;

* Paragraph 30(f) that requires profits and losses of a statutory fund to be dealt with in accordance with Divisions 5 and 6 is replaced by a requirement that surpluses in an approved benefit fund be distributed in accordance with section 56 (see below); *Item 2 of Schedule 5*;

* In paragraph 38(2)(c) that refers to a distribution under Division 6 the reference is replaced with a reference to Division 5 (see below); *Item 7 of Schedule 5*;

* In subsection 38(7) the reference to Division 6 is being replaced with a reference to Division 5 (see below); *Item 8 of Schedule 5*;

* In subsection 45(1) the reference to Division 6 is being replaced with a reference to Division 5 (see below); *Item 9 of Schedule 5*;

* Part 4, Divisions 5 and 6 is being substituted with a new Division 5 (section 56) of Schedule 1 that deals with the distribution of surplus in approved benefit funds; *Item 10 of Schedule 5*.

- The provision enables a society to pay, apply or allocate all or part of the surplus to the members of the approved benefit fund, or transfer all or part of the surplus to another approved benefit fund or to the management fund if the rules of the society so provide.

The appointed actuary must advise the friendly society that there is a surplus before the distribution can take place. The distribution must comply with any applicable prudential standard.

- Prudential Standard 2 (Benefit Fund Requirements) is introduced to set out the matters that the actuary's advice must include and the allowable methods of distributing or allocating benefit fund surplus. This standard has been based on the Australian Financial Institutions Commission (AFIC) Prudential Standard 6.6.2.g.

The Discontinuation of Directions upon Winding- Up

At present the Life Insurance Act provides that directions cease to have effect when an order is made for the winding-up of the life insurance company. At present a life insurance company is not to be wound up except by order of the Court on an application by a judicial manager (under subsection 175(6)) or on application by APRA (section 18 1). In addition, the Life Insurance Act

(subsections 180(2) - (4)) provides for a friendly society to be wound up voluntarily in specified circumstances.

Given the introduction of a voluntary winding-up process for friendly societies, the regulations extend the provisions of the Act dealing with the discontinuation of directions upon winding-up to also deal with the additional process for friendly societies. The regulations provide that, where a special resolution is passed for the voluntary winding-up of the society and APRA is notified, the direction will cease to have effect if APRA gives its written permission to the society. The following provisions of the Act will be modified in this manner:

- * subsection 68(8) dealing with solvency directions; *Item 11 of Schedule 5*;
- * subsection 73(8) dealing with capital directions; *Item 12 of Schedule 5*;
- * subsection 73F(9) dealing with management capital directions; *Item 13 of Schedule 5*;
- * subsection 134(4) dealing with directions regarding company assets; *Item 22 of Schedule 5*; and
- * subsection 150(9) dealing with directions during or after an investigation; *Item 23 of Schedule 5*.

Treatment of Financial Records and Statements

Division 2 of Part 6 of the Life Insurance Act establishes the requirements for a life insurance company's financial records. These provisions require the financial records to be divided into various classes (ie, ordinary or superannuation business), ' categories (ie, participating or non-participating, and Australian or overseas) and subcategories. As friendly societies generally adopt a single product benefit fund structure it is not possible to further divide the financial records of each benefit fund using the class and category structure described in Division 2 of Part 6 of the Life Insurance Act.

For this reason, the regulations disapply the requirements of sections 75 and 76 of the Life Insurance Act and reimpose the requirements of the Friendly Societies Code for financial records to be maintained for each management fund and approved benefit fund of the friendly society (Item 14 of Schedule 5).

Section 81 of the Life Insurance Act requires a life company to treat as an amount of income or outgoing the appreciation or depreciation of an asset. This would require a friendly society to apply market value accounting for accounts prepared for the management fund as well as all benefit funds. Under the Friendly Societies Code, market value accounting is only required for certain assets (principally traded securities) held by the management fund. Items 15 and 16 of Schedule 5 of the principal Regulations modify the requirement in section 81 by providing that an asset of a management fund only need to satisfy the requirements of section 81 if the Prudential Rules so require. Prudential Rule 47 provides that in accounting for the management fund, only traded securities are required to be measured at net market value.

The regulations also introduce transitional provisions regarding the due date for the lodgement with APRA of financial statements in the first years after the transfer date. The arrangements reflect the longer timeframe to lodge financial statements under the Friendly Societies Code and provide a period of adjustment for friendly societies to meet the requirements of the Act. The transitional arrangements made in the regulations are as follows:

- * For financial statements for a financial year ending on or before the transfer date that have not been given to the SSA before the transfer date; at least 14 days before the end of 5 months after the end of the financial year to which the financial statements relate;

- This is consistent with the transitional provisions being made for the lodgement of financial statements under the Corporations Law (see Part 12.6 of the *Corporations Regulations 1990*);
- * For financial statements for a financial year ending between the transfer date and the end of 31 December 2000; within the period applying to the company for lodgement of its annual report under the Corporations Law;
- This provides a lodgement period of 4 months after the end of the financial year for friendly societies that are non disclosing entities for Corporations Law purposes;
- * For financial statements for a subsequent financial year; within 3 months after the end of the financial year to which the financial statements relate.
- This will end the transitional period and thereby bring the Life Insurance Act reporting requirements for friendly societies into line with those for other life insurance companies.

Modifications to the following provisions of the Life Insurance Act are set out in the regulations to provide these transitional arrangements:

- * Paragraph 82(5)(c) in respect to financial statements required at the end of each financial year;

Item 17 of Schedule 5;

- The transitional provisions do not apply to financial statements that may be required other than at the end of the financial year under subsection 82(2);
- * Subsections 118(3) and (4) in respect to financial statements and annual statistical returns; *Item 20 of Schedule 5*; and
- * Subsection 119(1) in respect to a financial condition report; *Item 21 of Schedule 5*.

Actuarial Investigations

Section 113 of the life Insurance Act requires a life insurance company's appointed actuary to investigate the financial condition of the company and provide a written report. Under the Friendly Societies Code, the actuarial investigation is to focus on each individual benefit fund with the investigation of the management fund limited to the extent that it affects the operations of the benefit fund. The requirements for the actuarial investigation of the management fund are established in AFIC Prudential Standard 6.6B. The Prudential Standard focuses on the operations of the management fund that are most critical to the benefit funds so that the actuarial report can be produced in a timely and efficient manner.

Consistent with the practice of the Friendly Societies Code, Item 18 of Schedule 5 clarifies that, for friendly societies, an annual actuarial investigation is required for:

- * each approved benefit fund of the society; and
- * the management fund, to the extent required by the prudential standards.
- Prudential Standard 1 (Actuarial Advice) sets out the requirements for the appointed actuary's actuarial investigation. This Prudential Standard is based on AFIC Prudential Standard 6.6B. Prudential Standard 1 requires the appointed actuary to only consider the management fund to the extent it affects the operation of the approved benefit funds. Exceptions to this are the need for the actuary to consider retirement villages, expense analysis, derivatives use or

where more extensive investigation is required as a result of the risk profile of the management fund.

Section 115 of the Life Insurance Act ensures that a life insurance company is not prevented from having its appointed actuary investigate its financial condition at a time other than the end of the financial year. Consistent with the modifications in Item 18 of Schedule 5 with respect to section 113, Item 19 of Schedule 5 modifies section 115 to ensure that an additional financial condition report can be undertaken for each approved benefit fund and the management fund of the friendly society (to the extent required by the prudential standard).

Members Registers

Sections 226 and 227 of the Life Insurance Act require a life company to maintain a register of policies for each jurisdiction in which it carries on life insurance business and set out the requirements for the register. Information about the State or Territory residency of policy owners obtained from the registers is used for purposes such as ensuring notices are posted in relevant State newspapers in the case of a transfer of amalgamation of life insurance business under Part 9 of the Life Insurance Act.

In comparison, friendly societies maintain registers of benefit members of each benefit fund (subsection 318(2) of the Friendly Societies Code). Item 29 of Schedule 5 modify the requirements of the Act so that friendly societies continue to keep a register of each approved benefit fund of the society as per the requirements of the Friendly Societies Code. The regulations introduce a requirement for the register to be kept in parts for each State or Territory. A friendly society that does not already keep its register in this manner will need to comply within 18 months from the transfer date (or a longer period allowed by APRA in writing). Item 30 of Schedule 5 omits the requirements of section 227 of the Act for friendly societies.

Section 242

Section 242 of the Act provides for postal voting by members of a mutual life insurance company in respect to the election of **directors and amendments** to the company constitution. All friendly societies **are presently mutual organisations and would thus be subject to section 242**. However, other requirements in the Act and the Corporations Law serve to involve members in the governance of **the company**:

- * Part 2A of the Act establishes a process for amendments to approved benefit fund rules, which form part of the company's constitution.
- * Recent reforms of the Corporations Law provide for proxy voting and enable a member to specify the way the proxy is to vote on a particular resolution (Division 6 of Part 2G.2).
- * The Corporations Law allows a company's constitution to establish the process used for the appointment of directors, including a postal ballot (section 228(10)).

As there are other processes that achieve a similar outcome to section 242, Item 32 of Schedule 5 disappplies section 242 in its entirety to friendly societies.

Schedule - Dictionary

Items 33 to 36 of Schedule 5 include definitions of terms that will be introduced into the Life Insurance Regulations. Subject to the following explanation, the definitions are self-explanatory:

- * *management fund* - the definition is similar to that used in section 16K of the Life Insurance Act. However, the proposed definition in the regulations will provide that the assets and liabilities of a *health benefits fund* do not form part of the management fund of the society.

This is relevant because Schedule 6 of the principal Regulations will deal with jointly regulated friendly societies that operate both health benefits funds and approved benefit funds.

New Schedule 6 - Further modifications of the Act in relation to jointly regulated friendly societies

Item 16 also inserts a new Schedule 6 into the Life Insurance Regulations to further modify the Life Insurance Act in relation to jointly regulated friendly societies.

Monitoring jointly regulated friendly societies

Item 1 of Schedule 6

Item 1 of Schedule 6 modifies section 127 of the Life Insurance Act by providing that a person who may be appointed as an inspector under section 82R of the *National Health Act 1953* (National Health Act), may be appointed as an *authorised person* for the purposes of Part 7 of the Life Insurance Act (i.e. the monitoring and investigation powers). This allows persons with expertise in regard to health insurance business to be appointed by APRA or ASIC to assist in monitoring or investigating the activities of jointly regulated friendly societies.

Item 2 of Schedule 6

These modifications expand the purpose of Division 2 of Part 7 of the Life Insurance Act to enable the Regulator to monitor the extent of compliance by a jointly regulated friendly society with certain legislative and other requirements pertaining to its health insurance business.

Item 3 of Schedule 6

This modification to section 131 of the Life Insurance Act ensures that the Regulator may also give a jointly regulated friendly society a written notice requiring the society to give it information about its health insurance business.

Investigation and directions for jointly regulated friendly societies

Item 4 of Schedule 6

This item modifies the definitions of certain key concepts that apply throughout Division 3 of Part 7 of the Life Insurance Act (that deals with investigation by the Australian Prudential regulation Authority (APRA)). Accordingly, the terms **life insurance business** are taken to include health insurance business and policy will be taken to include a health insurance policy. The effect of these definitional modifications is to allow the investigation and directions powers of the Division to also apply to the health insurance business of jointly regulated friendly societies.

Item 5 of Schedule 6

Proposed subsection 134(1A) specifies that directions may be given by the Regulator in respect of assets of approved benefit funds (including health benefit funds) established for each type of business of a jointly regulated friendly society. This recognises that the 'respective benefit funds' are established to fund the liabilities of policies referable to that fund in accordance with the benefit fund rules. In so far as a direction is to be given in respect of the assets of either type of benefit fund (ie. for life or health), it should be given only if the interests of owners of policies referable to that fund are served by it being given. For example, a direction over the assets of a health benefit fund should not be given to preserve the jointly regulated friendly society's ability to meet liabilities to life insurance policy owners.

Moreover, subsection 134(1B) provides that APRA must not give a direction that relates to an asset of a health benefit fund without the written approval of the Minister for Health and Aged Care or PHIAC.

Item 6 of Schedule 6

This item establishes additional grounds upon which a show cause notice may be given that mirror those grounds for investigating health insurance business under the National Health Act. Where a jointly regulated friendly society contravenes the National Health Act, its regulations, conditions of registration under that Act, directions given under that Act, the *Private Health Insurance Incentives Act 1997* or the *Private Health Insurance Incentives Act 1998*, subparagraph 136(b)(iii) enables its health insurance business to be investigated under the Life Insurance Act.

Item 7 of Schedule 6

Following the issue a **show cause notice**, the Regulator must decide whether to proceed to investigate a - life company under the Life Insurance Act. Where an investigation will involve the health insurance business of a jointly regulated friendly society, and the society has not consented to an investigation, proposed subsection 137(3) requires the Regulator to obtain the written approval of the Minister for Health and Aged Care or PHIAC before deciding to investigate the jointly regulated friendly society.

Item 8 of Schedule 6

Investigations of the health insurance business of a jointly regulated friendly society could alternatively occur under the National Health Act. This modification provides that only one investigation is able to proceed at any particular time. Therefore this Item precludes an investigation of a jointly regulated friendly society commencing under the Life Insurance Act if an investigation in respect of that society is in progress under the National Health Act. However, the regulators may agree to an existing investigation being broadened to encompass the other type of business, or cancelled to allow a broader investigation to commence.

It is intended that parallel regulations will be made under the National Health Act to provide for the reverse case i.e. to preclude an investigation commencing under the National Health Act in respect of a jointly regulated friendly society where one is already underway under the Life Insurance Act.

Items 9 and 10 of Schedule 6

These items modify section 149 of the Life Insurance Act to ensure that where an investigation has involved the health insurance business of a jointly regulated friendly society, the report of the investigator must contain relevant opinions and recommendations about the conduct of the health insurance business. In such a case, the opinions and recommendations must also to be given to the Minister for Health and Aged Care and PHIAC (and may be given to the Registration Committee established under section 70 of the National Health Act). The relevant person will then consider whether further action is appropriate with respect of the health insurance business under the Life Insurance Act. Alternatively, the Minister for Health and Aged Care or PHIAC may decide to take action in respect of the health insurance business under the National Health Act.

Items 11 and 12 of Schedule 6

These items broaden the conditions under which directions may be given under section 150 of the Life Insurance Act to mirror the modifications in Item 6 of Schedule 6. The modifications provide that where an investigation is underway or has been conducted, and a jointly regulated friendly society has breached certain legislative and other requirements pertaining to its health

insurance business, the Regulator may issue written directions in accordance with section 150. However, a direction must not be given that affects the health insurance business of a jointly regulated friendly society without the written approval of the Minister for Health and Aged Care or PHIAC.

Judicial management of jointly regulated friendly societies

The judicial management of a jointly regulated friendly society will generally occur under the Life Insurance Act, as provided by section 162. Where judicial management is to proceed only in respect of the health insurance business, the modifications will allow the process to occur under the National Health Act.

Item 13 of Schedule 6

These items modify the definitions of certain key concepts that apply in Division 1 of Part 8 of the Life Insurance Act. Accordingly, business is taken to include health insurance business; **and policy** is taken to have a variable definition depending on the context and the type of business to which the relevant provisions apply. The effect of these definitional modifications is to allow judicial management to proceed over either the life insurance business (i.e. policies as defined by subsections 16F(1) or (2) of the Life Insurance Act) in isolation or over the entire jointly regulated friendly society, including its health insurance business.

Item 14 of Schedule 6

Subsection 157(1A) is inserted to require APRA to obtain the written approval of the Minister for Health and Aged Care or PHIAC before applying to the Court for an order for judicial management of all, or a part of the business (that includes its health insurance business), of a jointly regulated friendly society.

Item 15 of Schedule 6

Where a jointly regulated friendly society applies for a Court order for judicial management in accordance with modified section 157 of the Life: Insurance Act, PHIAC and the Minister for Health and Aged Care are entitled to be heard by the Court.

Item 16 of Schedule 6

Section 158 provides for the Court, in determining whether to appoint a judicial manager to a jointly regulated friendly society, to consider the results of an investigation under either the Life Insurance Act or National Health Act.

Items 17 and 18 of Schedule 6

Modifications to section 159 will allow the Court to place a company under judicial management in response to breaches of key requirements of the National Health Act, e.g. the solvency standard or conditions of registration. The modification to paragraph 159(b) ensures that a Court may order the judicial management of a jointly regulated friendly society in circumstances where there may be insufficient time to conduct an investigation under Part 7 of the Life Insurance Act or section 82R of the National Health Act.

Items 19 and 20 of Schedule 6

Modifications to section 162 will allow the health insurance business (only) of a jointly regulated friendly society to be placed under judicial management in accordance with the National Health Act.

Item 21 of Schedule 6

This item inserts a new section 166A which is similar to section 166 of the Life Insurance Act to ensure that a jointly regulated friendly society is still bound by the relevant provisions of its governing legislation despite being placed under judicial management. Section 166A requires a jointly regulated friendly society to comply with provisions of the National Health Act despite the appointment of a judicial manager.

Item 22 of Schedule 6

Modifications to section 167 will provide that APRA, the Minister for Health and Aged Care and PHIAC is entitled to be heard when the Court considers an application by the judicial manager for instructions in relation to the judicial management.

Item 23 of Schedule 6

Modifications to section 169 give the Minister for Health and Aged Care and PHIAC a right to be heard in cases where APRA applies to the Court for instructions to be given to a judicial manager that affect the health insurance business of a jointly regulated friendly society.

Item 24 of Schedule 6

Modifications to section 170 allow the Minister for Health and Aged Care and PHIAC to seek information from a judicial manager regarding the conduct of judicial management that relates to the health insurance business of a jointly regulated friendly society. The modifications require the judicial manager to comply with the request.

Item 25 of Schedule 6

Modifications to section 172 ensure that the Minister for Health and Aged Care and PHIAC are entitled to be heard by the Court when it considers an application for the cancellation of judicial management that relates to the health insurance business of a jointly regulated friendly society.

Items 26, 27 and 28 of Schedule 6

Modifications to section 175 will provide that, for jointly regulated friendly societies, the judicial manager may also recommend that the health insurance business be transferred to another registered body or that individual health benefit funds be wound up under the National Health Act. The modifications in respect of transferring business do not limit the other courses of action that a judicial manager may recommend. The modification of subsection 175(4) ensures that a Court is able to make orders in accordance with the recommended course of action.

Winding-up of jointly regulated friendly societies

There are to be four alternative procedures be available for liquidating a jointly regulated friendly society, or part thereof

Voluntary winding-up under subsections 180(2), (3) and (4) of the Life Insurance Act;

- * Upon application by APRA under section 181 of the Life Insurance Act;
- * Upon an order of the Court under section 176 of the Life Insurance Act; and
- * Individual health funds may be liquidated under National Health Act.

The modifications set out in this Regulation relate only to the Life Insurance Act processes, except insofar as they do not preclude the fourth alternative under the National Health Act.

Item 29 of Schedule 6

This item modifies certain key definitions used in Division 2 of Part 8 of the Life Insurance Act relating to the winding-up of life insurance companies. Accordingly, **policy** is taken to include a health insurance policy. The effect of this definitional change is to ensure that a jointly regulated friendly society may be wound up in accordance with processes under the Life Insurance Act.

Item 30 of Schedule 6

This modification will enable individual health benefits funds to be wound up in accordance with the National Health Act.

Items 31 and 32 of Schedule 6

This modifications to section 181 requires APRA to obtain the written approval of the Minister for Health and Aged Care or PHIAC (as well as meeting the other requirements of section 181) before applying to a Court for a jointly regulated friendly society to be wound-up under the Life Insurance Act.

Item 33 of Schedule 6

This modification to section 183 will allow PHIAC and the Minister for Health and Aged Care to be heard on the application to a Court by a liquidator in relation to a matter arising under the winding up of a jointly regulated friendly society. This involvement may only relate to the health insurance business of that jointly regulated friendly society.

Item 34 of Schedule 6

This modification to section 184 will allow PHIAC and the Minister for Health and Aged Care to be heard on the application to a Court by APRA for directions concerning the winding-up of a jointly regulated friendly society. This involvement may only relate to the health insurance business of that jointly regulated friendly society.

Item 35 of Schedule 6

This modification to section 185 allows PHIAC and the Minister for Health and Aged Care to ask a liquidator for information in writing about the winding-up of a jointly regulated friendly society. Such requests may only relate to the health insurance business of that jointly regulated friendly society.

Item 36 of Schedule 6

This modification to section 186 will ensure that, in determining a jointly regulated friendly society's liabilities to policy owners, the liquidator is required to take account of the relevant approved benefit fund rules for each type of policy owner. The liquidator must only take account of the health benefit fund rules to the extent that those rules are consistent with any directions of the Court.

Item 37 of Schedule 6

The general order of priority that exists under the Life Insurance Act for the application of statutory fund assets on winding-up is intended to be preserved. That is, the modified

subsections 187(1) and (2) require the assets of the fund to be applied in accordance with the Corporations Law in discharging the debts and claims referred to in subsection 556(1) of that Law to the extent that those debts are liabilities referable to the approved benefit fund or the health benefits fund.

For remaining assets, the modifications to section 187 ensures that all policy owners are placed on an equal footing when a jointly regulated friendly society is liquidated. That is, each policy owner have claims over the assets of their respective fund (ie the approved benefit fund or health benefit fund) in accordance with the approved benefit fund rules of that fund. The modifications ensure that the remaining assets of respective benefit funds are first used to extinguish the liabilities of the owners of policies referable to that fund. Any further assets will be distributed in accordance with the modified subsection 187(3) so as to firstly discharge other liabilities of the business of the fund and secondly applied in such manner as the Court directs (which is to be equitable and follow the requirements set out in modified subsection 187(4)).

Item 38 of Schedule 8

Modifications to section **188 provide that directors** may be liable for losses, in certain circumstances, to both health benefits funds and (life insurance) approved benefit funds. The objective of this modification is to invoke equal protection of the health insurance and life insurance funds.

Transfers and amalgamations of business of jointly regulated friendly societies

It is proposed that there will be three separate mechanisms for transferring and amalgamating the business of jointly regulated friendly societies.

- * Part 9 of the Life Insurance Act is modified to allow both life insurance business and health, insurance business of jointly regulated friendly societies to be transferred or amalgamated in accordance with a Court endorsed scheme.
- * The *Financial Sector (Transfers of Business) Act 1999* provides for the life insurance business of jointly regulated friendly societies to be transferred in accordance with that Act.
- * The National Health Act allows health insurance funds to be transferred in accordance with that Act (subject to Court endorsement).

These modifications in this regulation affect Part 9 of the Life Insurance Act only.

Item 39 of Schedule 6

The modifications to section 190 are intended to provide that Part 9 of the Life Insurance Act may also be used to transfer the health insurance business of a jointly regulated friendly society under a scheme confirmed by the Court.

Alternatively, the health insurance business may be transferred in accordance with section 82ZF of the National Health Act.

Items 40 and 41 of Schedule 6

These modifications to section 191 require a copy of the scheme and any actuarial report to be given to the Minister for Health and Aged Care or PHIAC where a health benefit fund of a jointly regulated friendly society is affected by a scheme prepared for the purposes of a transfer or amalgamation under Part 9 of the Life Insurance Act. (See also the modifications to the related Regulation 9.01 in Item 7)

Item 42 of Schedule 6

The modifications to section 192 require APRA to give a copy of any actuarial report to the Minister for Health and Aged Care or PHIAC where a health benefit fund of a jointly regulated friendly society is affected by a scheme prepared for the purposes of a transfer or amalgamation. (See also the modification to note 2 of Regulation 9.02 in Item 8)

Item 43 of Schedule 6

The modifications to section 193 also give the Minister for Health and Aged Care and PHIAC a right to be heard by the Court where a company seeks confirmation of a Part 9 scheme prepared for the purposes of a transfer or amalgamation of a health benefit fund of a jointly regulated friendly society.

Item 44 of Schedule 6

The modifications to section 197 require that, upon transfer of any part of the health insurance business of a jointly regulated friendly society, the receiving body give documents to APRA in accordance with the regulations made under subsection 197(1).

Prudential Standards

Item 45 of Schedule 6

The modifications to section 230A require APRA to obtain the written approval of the Minister for Health and Aged Care or PHIAC before it determines, varies or revokes prudential standards in respect of a class of companies that only includes jointly regulated friendly societies.

Item 46 of Schedule 6

These modifications to the definition of policy owner for the purposes of section 230A ensure that the interests of health insurance policy owners and life insurance policy owners are equally considered where a prudential standard is to be determined by APRA.

Directions to jointly regulated friendly societies

Item 47 of Schedule 6

Modifications to section 230B provide additional grounds upon which APRA may issue directions to a jointly regulated friendly society.

Item 48 of Schedule 6

The modifications to the definition of policy owner for the purposes of section 230B ensure that the interests of health insurance policy owners and life insurance policy owners are equally considered where a direction is to be issued by APRA. The written approval of the Minister for Health and Aged Care or PHIAC is required before APRA gives a direction to a jointly regulated friendly society under section 230B that affects its capacity to conduct health insurance business.

Schedule - Dictionary

Item 49 of Schedule 6

This modification inserts a definition so that PHIAC is taken to mean the Private Health Insurance Administration Council.

