



BERMUDA MONETARY AUTHORITY

DISCUSSION PAPER

PROPOSED ENHANCEMENTS TO INSURANCE SUPERVISION AND ENFORCEMENT POWERS

FEBRUARY 2009

PREAMBLE

This paper relates to one of the projects laid out in the Bermuda Monetary Authority's ("BMA" or "the Authority") Business Plans 2008 and 2009. It is designed to consider whether there are any powers utilised by other regulators which might enhance the capacity of the Authority to effectively regulate the insurance industry, to ensure the Authority meets appropriate international standards, and to assist with mutual recognition under Solvency II.

Any consideration of additions to a regulator's powers needs to ensure that all material views are considered as part of the review process.

This Discussion Paper enables external stakeholders to gain an insight into our initial thoughts and comment at an early stage to allow the Authority to identify, implement and use of appropriate powers in the future.

This project builds upon work started by the BMA Legal Services and Enforcement Team, presented to the IMF for the review in 2007, and will consider the outcome of other initiatives currently underway within the Authority.

To align with the objective of relative harmonization of processes throughout the Authority's regulatory jurisdiction some of the issues will need to be considered in tandem with other current and future projects at the Authority, such as the Anti-Money Laundering ("AML") legislation and international developments.

Different proposals will be progressed independently in certain instances depending upon priorities. Subject to the progress of this discussion paper a similar paper on enforcement relating to Banking, Trusts and Investment issues and including generic perimeter issues, is to be published in late 2009.

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1 SUMMARY

- 1.1 The Authority has a number of supervisory and enforcement powers which it may use in its regulation of the insurance sector. Existing legislation provides for powers such as cancellation of licenses, the removal of senior officers, directors and controllers in some circumstances or the giving of directions to licensed entities. These powers are relevant to the most serious enforcement issues leaving a lack of more targeted powers for regulatory issues of a minor to medium nature
- 1.2 The Authority is reviewing its enforcement powers in insurance and is seeking to engage stakeholder views through this Discussion Paper. Our initiative is prompted by the significant growth in recent years of the Bermuda insurance market, the Authority's goal of developing as a leading risk-based financial regulator and the emerging international debate on effective regulation.
- 1.3 The timing of this review is opportune as the current events in the financial markets have given rise to a number of calls to review regulation, more specifically to strengthen regulatory powers. There is certainly a need to review, but only to strengthen processes if there is a gap that needs addressing. The fact that the initial work on this project was already underway when the significant worldwide market issues emerged is enabling the Authority to react in a considered manner.
- 1.4 As the Authority is a risk-based financial regulator, any changes to the powers available will be used accordingly. Following a risk-based methodology, we feel that the application of these powers is more likely to be appropriate to the commercial sector than the captive sector, however each case will be considered on merit.

Publication of Enforcement Action

- 1.5 Publication of enforcement activity by regulators is widespread in other jurisdictions and, to some extent, adverse inferences could be drawn from the absence of public enforcement activities. We have concluded that consideration should be given to the development of an express power for the Authority to publicise enforcement action taken and the appropriate policies to use it. **This proposal is being brought to the attention of all stakeholders in this paper as there is a strong argument for its application throughout the Authority's jurisdiction.**

Enforcement Powers Concerning Individuals

- 1.6 We have also reviewed our enforcement powers concerning individuals who take up positions as directors, officers or controllers. Currently the Authority must approve the appointment of such individuals at the licensing stage. The Authority has powers to remove or replace such individuals when certain specified events occur.

- 1.7 We have considered whether this power would usefully be supplemented by the power to require individuals in specified functions to register with the Authority or whether we should seek a power to ban individuals from acting in roles in the industry for a specified period utilising “fit and proper” criteria.
- 1.8 The Authority’s powers in this area could be misunderstood and are not consistent with powers in other regulatory regimes. We have, therefore, raised the proposition of a broad-based banning process for consideration.

Civil Fines

- 1.9 Whilst many regulators have the capacity to impose civil fines the BMA does not have this general power under the insurance specific legislation. This seems to represent a simple and effective regulatory tool and, following the introduction of such a power in the AML/Counter-Terrorism Financing (“CTF”) legislation, we have concluded that such a power may be appropriate as an enhancement tool in the supervision of the insurance industry.

Other Powers

- 1.10 We have identified a number of specific powers available in other jurisdictions and have described them in an abbreviated way. Each power seems to have merit, and afford the chance to use more focussed and targeted solutions to regulatory issues.

2 CURRENT POSITION

- 2.1 Historically formal enforcement of regulation has been available through fining following criminal prosecution. However the use of discussion, imposition of requirements to regain compliance and movement to winding up etc., have been widely used. Such arrangements have usually remained private between the Authority and the insurer or individual.
- 2.2 The size of the industry and proximity of all parties enabled the above arrangements to operate effectively allowing the island to evolve into a synergous marketplace. There has been a high level of cooperation which has been beneficial to both regulator and regulated.
- 2.3 However we now operate in a highly complex, inter-linked worldwide financial market where the boundary between the product types is increasingly blurred and there is more reported cross-border crime. This, combined with developments elsewhere in corporate governance and regulation, and the recent heightened concerns about effective and transparent insurance and financial regulation suggest Bermuda needs to review its position to maintain its reputation and be able to demonstrate its commitment to effective regulation.
- 2.4 Below is a copy of the schedule which was presented to the IMF in 2007, identifying relevant powers. "IA78" references the Insurance Act 1978.

	Power	Insurance business
1	Written Warnings or Notice from the Authority	IA78 Section 4 (3) Registration of an Insurer (imposition of conditions)
2	Orders to comply with instructions/ Directions to protect the interests of clients	IA78 Section 32 Powers of intervention
3	Reports from regulated entity	IA78 Section 29A Power to obtain information and reports
4	Fines	<i>N/a (but criminal penalties can be administered through a Court Process, or fining in lieu of action with Company consent)</i>
5	Barring or removal of control Parties	IA78 Section 30F Objection to new or increased control; Section 30G Contraventions by Controller; and Section 30H Objection to existing controller
6	Barring or removal of	IA78 Section 32 Powers of Intervention

	senior officials	
7	Replacing/restricting powers of managers, directors or controlling owners	IA78 Section 32 Powers of Intervention.
8	Imposition of a conservatorship	IA78 Section 37 Continuation of long-term business of Insurer in liquidation.
9	Suspension or withdrawal of license	IA78 Section 41 (1) cancellation of registration of Insurer.
10	Criminal penalties	Breaches of some provisions amount to an offence.
11	Urgent Restrictions	Covered within IA78 Section 32 Powers of Intervention.
12	Winding-Up	IA78 Section 35 Winding up on petition from the Authority.
13	Right of Entry/Power to obtain documents and/or information	IA78 Section 29A Power to obtain information and reports; Section 29B Power to require the production of documents; 30B Powers of entry.

- 2.5 While this schedule appears extensive it should be noted there are limitations on the exercise of many of the above powers. For example, the capacity to remove a Director is contingent on a breach of the Act, a significant risk of insolvency, a failure (potential or otherwise) to meet minimum criteria or being a controller against whom a Notice has been filed.

3 POWERS AVAILABLE TO OTHER REGULATORS

3.1 We have performed a gap analysis comparing Bermuda to other jurisdictions (each of which matches Bermuda in at least one area of its insurance market):

- a. Australia, Singapore, New York and UK for “commercial insurers”.
- b. Switzerland and Ireland for “mixed but mainly commercial insurers”.
- c. Guernsey, Vermont and Cayman Islands for “mainly captive insurers”.

3.2 We reviewed four areas in each domicile:

- a. If they could use public censure of companies or individuals.
- b. If they required the registration of individuals with key functions.
- c. If they could ban individuals from roles.
- d. If they had civil fining structure (they all had a criminal fining structure).

Jurisdiction	Public Censure	Registering Individuals	Civil Fines	Banning Individuals
Bermuda	No	No	No	Barring not banning
New York	Yes	No	Yes	Yes
Australia	Yes	No	Yes	Yes
UK	Yes	Yes	Yes	Yes
Switzerland	Yes	No	No (could confiscate profits)	Yes (within limits)
Ireland	Yes	Yes	Yes	Yes
Singapore	Yes	Yes	Yes	Yes
Guernsey	Yes	Yes	No*	Yes
Cayman	Yes	No	No*	Yes
Vermont	Yes	No	No	Yes

* financial penalties possible for late filing

3.3 In the above table:

- a. By “public censure” we mean that the enforcement action is made public under the jurisdiction’s procedures, usually by publication on the regulator’s website, in a press notice or press release.
- b. By “civil fine” we mean that the regulator, in its own right, can impose a financial penalty on an individual or company, or can sue, again in its own right, through the civil court system.
- c. The comparisons are based on “closest fit” when an exact match of terminology is not possible.
- d. This comparison is based on our internal research, and we would welcome comment from stakeholders regarding it.

Gap Analysis

3.4 There are noticeable anomalies in the grid:

- a. Bermuda does not publish its enforcement proceedings, whereas, in some format, the other jurisdictions can.
- b. Bermuda does not have the power to ban individuals from holding a position for a term or for life. We can bar someone from holding a particular position but they can apply to hold similar positions in other companies. If someone has been banned in a significant overseas domicile they can still apply to be a controller of a Bermuda entity.
- c. Bermuda is more aligned with the captive domiciles regarding civil fining. The imposition of financial penalties is particularly notable in its absence when compared to non-captive domiciles.
- d. Whilst Australia and New York have not followed the UK and Ireland into requiring a full register of “significant” employees for the company (Controlled Function regime in the UK) it is possible to access a list of individuals that have been subject to enforcement proceedings.

4 ISSUES

- 4.1 Bermuda has a strong reputation for effective and discreet supervisory regulation of the insurance industry. However, we believe it is an appropriate time in the development of the market to provide additional tools to allow more public enforcement action, through financial sanctions, censure and other powers.
- 4.2 We have reviewed the powers available to other regulators, particularly the Australian Prudential Regulation Authority in Australia (“APRA”), the Financial Services Authority in the United Kingdom (“FSA”), the Guernsey Financial Services Commission in Guernsey and the Singapore Monetary Authority.
- 4.3 We have also considered the powers available to the Authority under other legislation, particularly the Investment Business Act, and considered issues that have recently arisen in our regulatory activities generally. It should be emphasised that these powers are suggested as appropriate to improve the regulatory options available to the Authority. It is not submitted that current conduct by industry participants has given rise to a direct need for these powers.
- 4.4 Our initial assessment is that the Authority’s enforcement powers concerning licensed firms would be usefully supplemented by additional powers including the capacity to publicise breaches of regulatory obligations and related enforcement action, applying financial sanctions for breaches of regulatory obligations and the other powers set out below. We make these proposals on the following grounds: that such public powers provide strong deterrent value; they are visible and easily understood examples of Bermuda’s commitment to effective regulation, they are consistent with a more transparent supervisory regime; they provide a wider range of tools to ensure effective risk-based supervision and they are more in line with the range of powers available in other major financial centres.
- 4.5 We have identified the following powers as particularly worthy of consideration:

Publicity of Regulatory Actions

- 4.6 Publicising enforcement and other regulatory activity is widely recognised as an effective tool for a regulator. It demonstrates the regulator’s activities and commitment to effective compliance with its policies to the financial industry, the jurisdiction and the world at large, and also serves as a significant deterrent to regulated entities when compliance with the legislation could occur. To date there has been no publicly available policy statement from the Authority on how it will approach the question of publicising its enforcement activities.
- 4.7 The development of such a policy, including the public discussion involved and subsequent implementation, would have the potential for significant deterrence, and promulgate compliance of regulated entities. It is noted that the current Act dealing

with AML compliance has a provision giving the Authority the power, but not the obligation, to publish details of any financial penalty imposed under that Act.

- 4.8 It is also noted that Sections 53 to 60 of the Investment Business Act (IBA) set out a legislative scheme enabling the Authority to publicise its opinion where it believes an investment provider has contravened a requirement imposed on it by the Act. The process is a complex one and the final outcome is governed by Section 60(5) of the IBA which prohibits publication if the Authority considers it would be “unfair to the person in respect to whom the action was taken or prejudicial to the interests of clients or potential clients of investment providers”.
- 4.9 Consideration would have to be given to the current confidentiality obligations imposed on the Authority under the various regulatory Acts. It is felt that the development of a formal policy, appropriate legislation and implementation has the potential to raise the visibility and transparency of the Authority’s regulatory regime and thereby enhance external confidence in Bermuda’s system of financial regulation. The Authority has highlighted transparency in its Business Plan and is committed to transitioning to a more transparent regime.
- 4.10 The Authority views this as a matter of priority with application beyond the insurance sector. Subject to the outcome of this consultation, this issue will be progressed separately to the other issues discussed in this paper.
- 4.11 Many Bermuda companies already “self-disclose” because of the listing rules on various exchanges, the requirements of SEC or similar rules for filings and due to accountancy requirements in the notes to the accounts. Therefore the change is not as great as some may feel.
- 4.12 This power would align us with comparable jurisdictions which would assist in the aim stated in the Business Plan that the Authority can ensure Bermuda’s regulatory framework is recognised as equivalent by other key jurisdictions and that our regulatory activities are demonstrable.

Regulation of Individuals

- 4.13 Certain individuals are required to be registered with the BMA. Section 8B of the Insurance Act requires the Authority to approve an actuary. Section 10 requires insurance managers and agents to be registered. Auditors must be approved pursuant to Section 16. There is no requirement for a principal representative to be registered, though they do have to be approved by the Authority under the Insurance Act 1978 Section 8(1B), no approval is required for the appointment of directors, underwriters or other senior personnel. When considering whether to approve applications for registration by institutions the Authority does evaluate the fitness and propriety of directors, other senior officers and known shareholders for the relevant position.

- 4.14 Under Sections 30D to 30I of the Insurance Act the BMA can serve a Notice of Objection to a “controller” of an insurer where it appears to the Authority that the individual is no longer fit and proper to hold that position. The definition of “controller” includes a managing director and a chief executive of the insurer as well as persons who hold various percentages of shares in the insurer in excess of 10%. It is an offence to continue as a controller after service of the Notice. There is also a provision which permits the BMA to apply to the Court for Orders compelling the sale of shares held by a controller.
- 4.15 Under Section 32 the BMA can issue a number of specified directions to an insurer if certain pre-conditions exist. Those pre-conditions are:
- a. If there is a significant risk that the insurer may become insolvent due to the way the business is being conducted.
 - b. The insurer is in breach of the Act or a condition imposed on it.
 - c. The minimum criteria of the insurer are not fulfilled or a person has become, or remained, a controller after a Notice of Objection has been served.
- 4.16 Amongst the specified directions that can be given the BMA may direct that a controller or officer be removed. Officer is defined to include a director, a secretary, chief executive or senior executive (which in turn is defined as a person who exercises managerial functions or is responsible for maintaining accounts or other records).
- 4.17 It can be seen that the BMA has some powers to remove certain individuals from the management of an insurer on the basis of their fitness and propriety and also a power to remove a wider class of persons if certain, specific pre-conditions have been met. There is no single overarching power available to remove any officer on the basis of their fitness and propriety.
- 4.18 There are a number of issues to be resolved in considering possible enhancement of the BMA’s powers in relation to the regulation of individuals.
- 4.19 The first is whether different roles should be distinguished in the regulation. There are a variety of roles involved in the management of an insurer and the position is complicated when Bermuda management is delegated to principal representatives. It is the BMA’s view that the highest standards of propriety and fitness should be demanded of all persons involved in the senior management of an insurer, irrespective of whether they are directors, senior executives, actuaries, underwriters or principal representatives, either individually or as part of a corporate structure.
- 4.20 The next issue to be considered is whether there should be a licensing structure, i.e. should the BMA have a power to authorise an individual to hold specified positions in an insurer or in the insurance industry generally. Given the multiplicity of roles,

the variety of qualifications and the fact that some individuals will be carrying out their responsibilities outside of Bermuda this is not considered a viable proposition.

- 4.21 If it is accepted that any regulatory power should extend to all of senior management and that it should not include a licensing system, then it follows that the appropriate form of regulatory power should be a “banning” power, i.e. a power to prohibit an individual from being a senior manager.
- 4.22 If such a power is to be given to the BMA, what would be the grounds for banning an individual? It is suggested that any process should be based on conduct which demonstrates the individual is not fit or proper to hold a senior role. To some extent triggers for the use of the power can be identified. For example, in Australia there are fitness and propriety standards prescribed in regulation. It is not however possible to exhaustively list the conduct which may trigger the use of such a power.
- 4.23 The current powers, set out above, relate to exclusion from the activities of a specific insurer. If a further power is to be granted to the BMA as set out above, seems that there is no logical reason to limit the “ban” to a specific entity. If an individual is unfit to hold a senior position in one insurer then it cannot be argued that that he is fit to hold similar positions with any other insurer. It is submitted, therefore, that any power should extend to a banning from the industry generally, rather than from a specific entity.
- 4.24 The preferred methodology is an internal process, similar to that recently introduced in the AML legislation. If the Authority formed the view that the conduct of an individual raised questions as to his fitness and propriety, a form of Notice would be issued, advising of the preliminary view, enclosing the material on which that view has been reached, and inviting a response. The Notice, material and response would be submitted to a senior officer of the BMA to make a decision whether to prohibit the individual from senior roles generally in the Bermuda Insurance Industry. There would also be an appeal process to an external tribunal.
- 4.25 A further issue arises as to whether the power should be exercised generally, i.e. any ban should be unlimited as to time, with a discretion vested in the Authority to remove the prohibition at some future time. The alternative is to empower the Authority to make the ban for a specified period. It is submitted that the better course is to limit the period of the ban as this would enable the Authority to more accurately react to various levels of misconduct.
- 4.26 It will be appreciated that the above power carries serious consequences for any individual. There will be circumstances where conduct is unacceptable but not sufficiently grievous to warrant banning. It is suggested that, as an adjunct to a banning power, a power to formally admonish an individual should also be included. Such a power would carry with it the capacity to publish the admonition issued.

- 4.27 This issue will be progressed so that the principles developed as a result of this discussion will be incorporated in the Guidance due to be published on Fitness and Propriety in the third Quarter 2009, as outlined in the Business Plan.

Civil Fines

- 4.28 The power to impose on an entity, a financial penalty by way of a civil fine for a failure to comply with its regulatory obligations is a primary enforcement tool in those jurisdictions where the power exists. It is understood to have proven an extremely effective power. The power has a number of attractive characteristics, from a regulatory standpoint.
- 4.29 Firstly, it gives a timely response to an issue of a breach. The often time-consuming processes inherent in the preparation and prosecution of a public criminal prosecution are avoided and in lieu a fairly straightforward administrative process is substituted. Thus, the time between the breach and the imposition of the penalty can be significantly shortened. This is attractive for a number of reasons, including fairness and probable cost efficiencies.
- 4.30 Secondly, it has the capacity to be more directly tailored to both the size of the entity in question and the relative importance of the provision which was breached. The Authority would have an intermediate and risk-based enforcement tool short of the more severe and final powers such as revocation of an insurer's license. This is attractive, not only as a matter of equity and fairness but, if coupled with a power to publish the findings, it has the significant merit of indicating to the regulated community, and the public at large, the Authority's views; both as to the obligations of insurers and the gravity which the Authority attaches to specific breaches of those obligations. In addition, recognition can be given to ameliorating factors such as "self-reporting", co-operation and immediate rectification. It is, in fact, a tool capable of being fairly calibrated to the full circumstances of the breach.
- 4.31 The Authority has recently been given a power to impose financial penalties in the AML/CTF area and the relative merits of an administrative power of this kind were exhaustively debated during that process. It is envisaged that any similar power imposed under the Insurance Act contain the same provisions and processes as that developed in the AML/CTF area. Thus, there would be a right of appeal to an external tribunal, there would be a preliminary Notice process and an opportunity to make submissions before a decision was made.
- 4.32 It is intended that this proposal be reviewed after the AML/CTF powers have been in place for some time, so that a more accurate assessment of the power can be made. It is currently proposed that the maximum size of the penalty be at a similar level to that of the AML/CTF legislation, that is, \$500,000.

Penalty Powers Regarding Notification and Filing Obligations

- 4.33 Most similar jurisdictions have provisions requiring the filing of various Returns and Notifications within prescribed times. Bermuda has such requirements in its regulatory Acts; however, unlike most other jurisdictions, failure to comply with those requirements, other than in a few specific instances, does not attract any penal consequences at all. This significantly detracts from the effect of the provisions and may encourage entities to ignore those requirements. It is suggested that a lack of sanctions for failure to lodge relevant returns, reports, certificates applications and notifications has the potential to severely impact on the Authority's knowledge of the entities it regulates, on the compliance of those entities with their obligations and the overall effectiveness of regulation.
- 4.34 One solution is to create a series of criminal offences for failure to comply with statutory requirements; however the criminal process is a lengthy and cumbersome method of dealing with what are, in most cases, minor breaches of obligation. In addition the criminal process conducted in open court has the potential to attract public attention and runs the risk of causing disproportionate harm to the entity's reputation compared to the offence committed.
- 4.35 In the United Kingdom failure to lodge a Return by the due date attracts a late payment fee of £250 as well as exposing the entity to possible further financial penalty. In Guernsey the Financial Services Commission Law empowers the Commission to make regulations for the charging of administrative financial penalties for failure to pay fees and the late filing of documents and information required under the regulatory laws. In the Cayman Islands there appears to be a "ladder of compliance" process which can escalate to the imposition of a penalty.
- 4.36 New York Insurance Department has a penalty for almost every late submission due to the regulator, which is comprehensively outlined on their website.
- 4.37 In Australia, there is a specific Act, known as the Financial Sector (Collection of Data) Act which authorises APRA to impose penalties for failure to lodge Returns and information as required. It should be noted the various regulatory Acts provide that it is an offence to fail to lodge Returns reports. The penalty provisions generally include a daily rate for outstanding returns as an option. The Act permits APRA to issue an Infringement Notice once it is satisfied an offence relating to lodgement of documents has occurred. That Notice specifies a Penalty, which is to be 20% of the maximum fine or 50 penalty units, (currently AU\$5,500). If the document is lodged and the penalty paid then no further action can be taken. If the penalty is not paid then APRA can refer the matter to the Director of Public Prosecutions for a formal prosecution and the issue is then dealt with before a Court. The process is identical to traffic fines.
- 4.38 The simplicity of the "flat rate" process in the United Kingdom has much to recommend it, however the implicit threat of wider penalties if there is an ongoing breach is not currently available in Bermuda. Obviously, if there is to be a general civil fining power, see para 4.28 et seq, then this can be dealt with as an adjunct.

The Australian process, whilst more complex, has some advantages, one of which is the availability of a Court process, if entities are not satisfied with the Authority's view. Another benefit is the option of dealing with a breach of the legislation without automatic recourse to a public hearing.

- 4.39 Both the above options are predicated on the Authority having the power, at least at first instance, to impose the penalty. It is felt that this is a more effective method of dealing with minor regulatory issues than referral to another body, such as the Director of Public Prosecutions. The issue of who retains the penalties will arise, however as the payment of a penalty under an infringement notice is not a criminal penalty. It is considered that the Authority should retain this to partially offset the Annual Business Fees applied to all regulated institutions.

Injunctions to Restrain Conduct and Compel Compliance

- 4.40 The traditional method to compel compliance with the law is a provision which makes it a criminal offence to either do, or fail to do, something. There are a small number of such criminal offences in the Insurance Act. This process remains an effective long-term sanction, however, given the length of time it takes to initiate criminal proceedings and for those proceedings to ultimately be dealt with to completion, it lacks the immediacy needed to ensure compliance in the short term. The capacity to take immediate action is especially important in the field of financial regulation where significant financial harm can be caused in a very short time
- 4.41 Many regulators around the world have resolved this by a power to approach a Court seeking Court Orders which compel entities and individuals to either do something to comply with the regulators directions or cease and desist with conduct which is in contravention of the law or proper conduct. These Orders can often be obtained within a very short time frame and on an interim basis pending a hearing. These Orders can, subject to the legislation, be used to compel regulated institutions to comply with proper practices as well as to prohibit unauthorised or unlicensed bodies from carrying on regulated businesses or holding themselves out to be regulated or authorised. The Orders obtained can be quite wide in nature and can extend to Orders which freeze assets, provide information or refund monies to investors, for example.
- 4.42 The FSA has power under Sections 380 and 381 of the Financial Services and Markets Act 2000 to seek injunctions in the High Court. From the press releases on its website, it has used them both to restrain unauthorised activity and freeze assets. Section 27 of The Registration of Non-Regulated Financial Services Businesses (Bailiwick of Guernsey) Law, 2008 contains a power to seek injunctions in respect of unauthorised businesses, as does the Banking Supervision Law of that bailiwick. Further, the Bermuda Investment Business Act 2003 contains a power, (Section 62), that permits the Authority to seek an injunction where there has been a contravention of a requirement under that Act. It is noted the Court can also freeze

assets and make restitution orders where there have been profits generated by the illicit conduct or losses caused to others.

4.43 In Australia, there are injunction powers in two regulatory Acts, the Superannuation Industry (Supervision) Act, under Section 315 and under the Section 65A of the Banking Act. It is worth noting that the Banking Act provision extends to Orders prohibiting the use of specific words which are reserved in the Act for regulated entities.

4.44 It is felt a power to seek Court Orders of the nature discussed above would be potentially useful in relation to the insurance industry where, due to the electronic marketplace, funds can be moved, and obligations created in time frames much shorter than those involved in the traditional criminal prosecution processes.

Enforceable Undertakings

4.45 These are a form of agreement where an entity, or an individual, undertakes to the regulator to do, or cease doing, some specified activity relating to the operation of a regulated activity. The undertaking is voluntary, however it is expressed to apply for a specified period and, if it is not kept, the regulator has the power to apply to a Court for Orders that it is complied with. Subsequent failure may be treated as a contempt of Court.

4.46 The use of these undertakings is common regulatory practice in Australia and a number of regulatory authorities have provisions in their legislation. Undertakings are used in many instances as a method of resolving regulatory concerns without the need for: a) more formal investigation or, b) conclusions adverse to an entity. Often they amount to a settlement mechanism for resolving concerns or disputes and do not necessarily have to include an admission of impropriety on the part of the entity.

4.47 There is provision in other UK legislation, such as Section 71 of the Enterprise Act 2002, allowing the Office of Fair Trading to have a power to accept such Undertakings. There appears no direct equivalent within the powers of the FSA; however Chapter 5 of their Decisions Procedures and Penalties Manual does discuss processes to reach settlement of enforcement action, which include an agreement. It is felt that this power may have significant use as a method of resolving issues with entities, without escalating them to an otherwise unnecessary level.

Court Orders Which Compel Compliance

- 4.48 The Proceeds of Crime (Supervision and Enforcement) Act contains a provision, which entitles the Authority to approach the Court where an entity has failed to comply with a Notice to supply documents or information. The Court has the power to make Orders requiring the entity to comply with the Notice and/or take other steps to remedy the consequences of its failure to comply.
- 4.49 It is noted that a criminal proceeding simply penalises the offender, without actually acquiring the information originally sought. This provision has the merit of compelling an entity to actually comply with the Notice or commit contempt of the Court. The power has many similarities with injunction powers and the two powers could be effectively combined, should this be seen as a viable option.

Involvement in Liquidations and Winding-Up

- 4.50 There are circumstances in which the Authority may wish to take an active part in any winding up process of an insurer, including the examination of directors and officers as to the circumstances leading up to the Application to the Court, examination of the insurer's books and records and a variety of other matters. It is entirely conceivable that the winding up of an insurer, especially an involuntary one, may disclose breaches of the Act and obligations by officers and others. Unless the Authority has the power to be directly involved in the winding up process that information will not be available to it and any subsequent action against individuals, or entities, may be severely impeded. While the Authority may have the power to conduct its own investigation, it is undesirable to have parallel inquiries being conducted at the same time.
- 4.51 Therefore it is suggested that a more detailed provision which addresses the Authority's role and powers in respect of winding up of an insurer may be desirable to ensure that any misconduct is identified and dealt with effectively.

5 DISCUSSION POINTS AND REVIEW

- 5.1 We seek comments from all stakeholders on the above paper and seek specific answers to the discussion points below:
- a. What are your views on each of the above proposals?
 - b. Do you feel the Authority is lacking any other supervisory or enforcement powers?
 - c. Do you feel that the enforcement procedures, checks and balances and tribunal appeal provisions in the recent Anti-Money Laundering legislation is an appropriate precedent for consideration in the enforcement framework for insurance?
 - d. Do you consider international comparisons a legitimate justification for additional powers?
- 5.2 Your comments and suggestions are sought, in writing, on or before **31 March 2009**. All submissions will be considered before a determination is made to progress any proposal.
- 5.3 The above proposals require different levels of priority depending on their immediate importance and relevance to the current needs of the Authority. The issue of publicity for regulatory actions is obviously of general importance across the Authority's various responsibilities. That importance is increased at a time when there is significant scrutiny of the effectiveness, and validity, of regulatory regimes throughout the world. Accordingly and subject to the responses received to this paper, the Authority will seek to initiate the legislative process in the immediate future to enable it to publicise regulatory actions where it considers this appropriate.
- 5.4 The question of the suitability of individuals for senior positions in the industry gives rise to some complex issues, especially when their actions initiate concerns regarding fitness and propriety. Accordingly we are going to progress this topic via a policy statement, which it is anticipated will be issued in the third quarter of the year.
- 5.5 As indicated in the body of the paper, it is our view that many of the powers discussed herein may have a more general applicability than exclusively insurance regulation. The general question of enforcement powers obviously relates to other parts of the financial community as well as insurance. Accordingly it is intended to issue a consultation paper dealing with the other industries over which the Authority has responsibility in the fourth quarter of the year. It is anticipated that

that paper will also deal with ‘perimeter’ issues, that is, how to regulate the boundaries of the industries under supervision.

- 5.6 The present paper raises the possibility of acquiring a “fining” power similar to that in the recent Proceeds of Crime Regulations (Supervision and Enforcement) Act. This power is as yet untried and until it has been in operation for some time it would seem inadvisable to seek to replicate it in other legislation. Accordingly the Authority does not propose to initiate a legislative process until early 2010 in relation to this proposal.
- 5.7 The balance of the proposals will be progressed consistent with the Authority’s other priorities and resources

Please forward all comments either by email or in writing to:

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