



Australian Government

Private Health Insurance Administration Council

Education Programs 2009

Governance Standard for Private Health Insurers

Sydney, 23 September 2009

Melbourne, 24 September 2009

Perth, 30 September 2009



Today's Program

- 2.00 – 2.15:** Introduction and Welcome
- 2.15 – 3.15:** Overview of Governance and Directorship Practice
(Geoff Carter, Facilitator, AICD)
- 3.15 – 3.30:** Afternoon Tea Break
- 3.30 – 4.30:** PHIAC's Governance Standard
(Shaun Gath, CEO, PHIAC)
- 4.30 – 5.00:** Q&A
- 5.00 – 6.00:** Drinks and canapés
- 6.30 – 8.30:** Dinner



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Shaun Gath
CEO, PHIAC



Agenda

- Why has Council done this?
- Underlying themes and objectives
- Features of the Standard
- Commentary on key provisions
- PHIAC oversight and enforcement
- Questions



First, the news....

- The *Private Health Insurance (Insurer Obligations) Rules 2009* were made by the Council on 11 September 2009.
- They will commence on 1 January 2010.
- The final version of the Rules is in your pack and will shortly be on the internet (after registration with the Federal Registry of Legislative Instruments).
 - Like all rules and delegated legislation, the Rules must be tabled in the Senate and HofR and are subject to disallowance under the *Legislative Instruments Act 2003*. Until that occurs they are valid and enforceable.
- PHIAC has prepared a Regulatory Impact Statement (**RIS**) which is also in your pack. This examines the costs and benefits associated with the Rules in some detail and is recommended reading for all attending today. This will go on PHIAC's website shortly.



Why is the Council doing this?

- Three reasons:
 - because they can
 - because they should
 - because experience suggests that it is needed



Can...

Section 165-1 of the *Private Health Insurance Act 2007* provides:

- (1) The Private Health Insurance (Insurer Obligations) Rules may establish prudential standards relating to prudential matters for private health insurers.
- (2) Prudential matters are matters relating to:
 - (a) the conduct by private health insurers of any of their affairs in such a way as:
 - (i) to keep themselves in a sound financial position; or
 - (ii) not to cause or promote instability in the Australian private health insurance system; or
 - (b) the conduct by private health insurers of any of their affairs **with integrity, prudence and professional skill.**



Should....

- Industry standards for governance exist in a number of comparable sectors:
 - APRA Prudential Standard GPS 510: Governance (standard for the general insurance industry)
 - Australian Stock Exchange (ASX) Corporate Governance Principles and Recommendations (principles applying to listed companies)
 - Decisions of the courts on corporate governance (e.g. recent litigation involving ASIC and the former James Hardie directors)
- Clear where best practice lies, esp. comparable economies
- Parliamentary and industry expectation that this would occur
- Council's own firm conviction that this is an appropriate step



Experience...

- HIH (2001)
- Enron Corporation (2001)
 - *Sarbanes-Oxley Act* (2002)
- Teacher's Union Health (2003)
- AIG (2008)



PHIAC's view on CG

- Effective CG succeeds best when multiple dimensions interact effectively:
 - *Legal* (e.g. *Corporations Act 2001*, compulsory codes and standards and the common law)
 - *Institutional* (e.g. professional standards, codes of conduct, corporate values)
 - *Ethical* (personal moral commitment to correct and transparent behaviours)



Universal Themes

- Independence of thought and deed
- Transparency and integrity
- Procedures that are documented and followed
- Sceptical, but constructive, engagement
- Shared commitment linked to values of individual responsibility



Key features of PHIAC standard

- Based on APRA's General Insurance Standard 510
- Schedule 1 to the *Private Health Insurance (Insurer Obligations) Rules 2009*
- A binding standard:
 - “Council-supervised obligations” which will be overseen and, where necessary, enforced
- As with the APRA standard, a minimum standard
 - Describes the *minimum* that insurers will need to do.
 - They can set higher standards and are encouraged to do so.



1: Board composition/experience

- A board must have at least 5 directors.
- The directors must have a range of skills, knowledge and experience to understand collectively:
 - (a) risks to the private health insurer; and
 - (b) the insurer's legal and prudential obligations.
- Each director must:
 - (a) have skills that allow him or her to oversee effectively the management of the private health insurer; and
 - (b) contribute effectively to the board's deliberations and processes.
- A private health insurer must tell the Council about a change in board membership or change in the name or contact details of a director:
 - (a) within 28 days after the change; and
 - (b) in the approved form.



2: Independence

- A board must have a majority of non-executive directors at all times.
- If a board consists of 5 to 7 directors, it must at all times have at least 3 independent directors one of whom is the chairperson.
- If a board consists of more than 7 directors, it must at all times have at least 4 independent directors one of whom is the chairperson.
- The chairperson of a board must be an independent director.
- Independence not affected by:
 - being a director of a parent company of the insurer; or
 - being a director of another subsidiary of the parent company.



3. “Independent” if...

- Not an executive director (i.e. an management-level employee of the insurer) and:
- either:
 - free from a business or other association which could materially interfere with exercise of independent judgement, including not being:
 - a substantial shareholder of the insurer or an officer of, or otherwise associated directly with, a substantial shareholder of the private health insurer; or
 - an employee or a former employee in an executive capacity, of the insurer or another member of the group, and there has not been a period of at least 3 years between ceasing that employment and serving on the board of the insurer; or
 - has, within the last 3 years, been a principal of a material professional adviser or a material consultant to the insurer, or to another member of the group, or an employee materially associated with the service provided; or
 - is a material supplier or customer of the insurer or other group member, or an officer of or otherwise associated directly or indirectly with a material supplier or customer; or
 - has a material contractual relationship with the insurer or another group member other than as a director
 - Or have not been approved in writing by PHIAC as an independent director.



4: Chairperson

- (1) A person may only be chairperson of a board if he or she has not been the chief executive officer (or equivalent) of the private health insurer at any time during the previous 3 years.
- (2) PHIAC can approve a “non-independent” as chair.
- (3) However, if the position of chief executive officer (or equivalent) is unexpectedly vacated, the chairperson may serve in the role for up to 90 days w/o approval.
- (4) Approval from the Council is required if a chairperson seeks to serve as chief executive officer (or equivalent) for more than 90 days.



5: Residency

- (1) The majority of directors of Australian-owned private health insurers must ordinarily reside in Australia.
- (2) For foreign-owned private health insurers:
 - (a) at least 2 directors must ordinarily reside in Australia; and
 - (b) at least 1 of the directors mentioned in paragraph (a) must be an independent director.



6: Board charter

A board must have a charter in writing that:

- (a) sets out the roles and responsibilities of the board, committees and management of a private health insurer;
- (b) provides a structure for determining how board decisions are to be made;
- (c) encourages directors to exercise independent thinking and judgment in the discharge of their responsibilities; and
- (d) if the private health insurer is part of a corporate group — clearly documents how the board will interact with the group.



7: Delegation

- (1) A board may delegate its authority to a person or a committee.
- (2) A delegation under subsection (1) must be in writing and retained as a record by the private health insurer.
- (3) A board must:
 - (a) ensure there are procedures for it to monitor the exercise of delegations; and
 - (b) not abrogate its responsibilities through the use of delegations.



8: Board policies

- (1) A board must ensure that :
 - (a) the private health insurer has written policies to manage the insurer's risks; and
 - (b) the insurer has procedures for monitoring and evaluating compliance with key policies are in place and regularly reviewed.
- (2) If the private health insurer is part of a corporate group and applies group policies or carries out group functions, the board of the insurer must ensure that the group policies or functions are consistent with the business requirements of the insurer.



9: Performance reviews

- (1) A board must have a policy and procedures for annually assessing its performance against its objectives.
- (2) The policy and procedures must provide for an assessment of individual directors, board committees and the board collectively.
(Rules provide a number of examples of objectives)



10:Board renewal

A board must have a policy about board renewal that addresses how the board will renew membership to ensure that:

- (a) it remains open to new ideas and independent thinking; and
- (b) it complies with section 1 (composition and independence); and
- (c) consideration is given the length of time a director has served on the board, and whether this could affect his or her ability to perform his or her duties.



11: Audit committee

- (1) A private health insurer must have a board audit committee.
- (2) The functions of a board audit committee must include an objective, non-executive review of the effectiveness of the private health insurer's financial reporting and risk management framework.
- (3) A board audit committee need not undertake a review of risk management if there is another board committee undertaking this function.
- (4) A board audit committee must meet at least once a year and:
 - (a) have at least 3 members, all of whom must be non-executive directors; and
 - (b) have sufficient power to enable it to obtain all information necessary to perform its function; and
 - (c) give a report to the board of the insurer after each committee meeting.
- (5) The chairperson of the board audit committee must be an independent director.
- (6) The chairperson of the board may sit on the board audit committee but must not chair the committee.



12: Internal audit

- (1) A private health insurer must have an internal audit function that is adequately resourced and skilled for the size and corporate complexity of the insurer.
- (2) The board must be satisfied that:
 - (a) the internal audit function is independent; and
 - (b) internal audit processes are clearly documented and subject to regular review; and
 - (c) the internal audit function has unfettered access to all business operations of the insurer.



13: Transitional

- (1) On the commencement of the Governance Standard, that is not able to comply with the requirements of the Standard must write to PHIAC :
 - (a) identifying all provisions in the standard with which the insurer is not able to comply; and
 - (b) specifying a date by which they can comply.
- (2) Council must then approve a date for compliance.
- (3) The insurer must comply by the new date.



Oversight and Enforcement

- No point in having a standard if it is not overseen and enforced
- We expect the industry to be fully compliant on 1 January 2010
 - No reason to believe this cannot be achieved
 - The transitional arrangement is there if needed
- We will be checking compliance in the following ways:
 - Fund reviews
 - Compliance when there is an obligation to inform us (e.g. directors)
 - Reports and information we receive
- No present plans to run unannounced “spot checks” but we reserve that right if concerns emerge either with the industry as a whole or in certain sectors
- Breach is a breach of a “council-supervised obligation”.



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Questions