



ASIC

Australian Securities & Investments Commission

CONSULTATION PAPER 111

Compensation and financial resources arrangements for credit licensees

July 2009

About this paper

This consultation paper sets out ASIC's proposals to administer the new compensation and financial resources requirements for credit licensees.

We are seeking the views of potential credit licensees and representatives, consumers and insurers on our proposals.

About ASIC regulatory documents

In administering legislation ASIC issues the following types of regulatory documents.

Consultation papers: seek feedback from stakeholders on matters ASIC is considering, such as proposed relief or proposed regulatory guidance.

Regulatory guides: give guidance to regulated entities by:

- explaining when and how ASIC will exercise specific powers under legislation (primarily the Corporations Act)
- explaining how ASIC interprets the law
- describing the principles underlying ASIC's approach
- giving practical guidance (e.g. describing the steps of a process such as applying for a licence or giving practical examples of how regulated entities may decide to meet their obligations).

Information sheets: provide concise guidance on a specific process or compliance issue or an overview of detailed guidance.

Reports: describe ASIC compliance or relief activity or the results of a research project.

Document history

This paper was issued on 15 July 2009 and is based on the National Consumer Protection Bill as at 25 June 2009

Disclaimer

The proposals, explanations and examples in this paper do not constitute legal advice. They are also at a preliminary stage only. Our conclusions and views may change as a result of the comments we receive or as other circumstances change.

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The consultation process

You are invited to comment on the proposals in this paper, which are only an indication of the approach we may take and are not our final policy.

As well as responding to the specific proposals and questions, we also ask you to describe any alternative approaches you think would achieve our objectives.

We are keen to fully understand and assess the financial and other impacts of our proposals and any alternative approaches. Therefore, we ask you to comment on:

- the likely compliance costs;
- the likely effect on competition; and
- other impacts, costs and benefits.

Where possible, we are seeking both quantitative and qualitative information.

We are also keen to hear from you on any other issues you consider important.

Your comments will help us develop our policy on compensation and financial resources arrangements for credit licensees. In particular, any information about compliance costs, impacts on competition and other impacts, costs and benefits will be taken into account if we prepare a Business Cost Calculator Report and/or a Regulation Impact Statement: see Section E, 'Regulatory and financial impact'.

Making a submission

We will not treat your submission as confidential unless you specifically request that we treat the whole or part of it (such as any financial information) as confidential.

Comments should be sent by Wednesday 12 August 2009 to:

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What will happen next?

Stage 1	15 July 2009	ASIC consultation paper released
Stage 2	12 August 2009	Comments due on the consultation paper
	August 2009 – October 2009	Drafting of regulatory guides
Stage 3	November 2009	Regulatory guides released

A Background to the proposals

Key points

The National Consumer Credit Protection Bill 2009 (National Credit Bill) states that credit licensees (other than those that are also regulated by APRA) must have:

- adequate financial resources; and
- adequate arrangements in place for compensating consumers.

To comply with the financial resources requirement, credit licensees must determine what financial resources will be adequate in their circumstances.

To comply with the compensation requirement:

- compensation arrangements must cover loss or damage suffered because of breaches of the National Credit Bill (as enacted) by the licensee or its representatives; and
- these arrangements are expected to be professional indemnity insurance cover that is adequate. ASIC may also approve alternative arrangements.

In this consultation paper, we set out proposals about what we will expect of credit licensees under the proposed new requirements.

Regulation of consumer credit

- 1 The Council of Australian Governments (COAG) agreed on 3 July 2008 that the Commonwealth would assume responsibility for the regulation of consumer credit. The Australian Government introduced the National Consumer Credit Protection Bill 2009 (National Credit Bill) into Parliament on 25 June 2009.
- 2 Regulation of consumer credit in the new regime will be the responsibility of ASIC. A key component of the new credit regime is that businesses that provide credit services or who are engaged in other ‘credit activities’ will be subject to financial resources and compensation requirements. For convenience, this consultation paper deals with ASIC’s administration of both the financial resources requirement and the compensation requirement.
- 3 This consultation paper is based on the National Credit Bill. We will monitor the progress of the Bill, and will revise our proposals if the requirements materially change before they are finally enacted. Our final position will be published in one or more Regulatory Guides later this year and will be based on the final legislation as passed by the Australian Parliament.

Note: A copy of the National Credit Bill may be downloaded from the Australian Parliament website at www.aph.gov.au/bills/index.htm.

What are the legislative requirements?

- 4 All credit licensees (other than those that are also APRA-regulated) must comply with the financial resources and compensation requirements. They therefore apply to lenders that are not authorised deposit-taking institutions (ADI) and non-lenders (such as finance brokers, mortgage brokers, credit advisers and loan advisers).
- Note: A 'lender' is a person who provides credit where the National Credit Code applies (the National Credit Code is Schedule 1 to the National Credit Bill) or who falls within the definition of cl 10 of the National Credit Bill. A 'non-lender' includes credit licensees that are either intermediaries (as defined in cl 9 of the National Credit Bill) or a person who provides credit assistance in accordance with cl 8 of the National Credit Bill.
- 5 These credit licensees must have adequate resources and have adequate risk management systems: see cl 47(1)(1). Financial resources and compensation arrangements are important to the management of risk. Credit licensees will need to assess their business and form a view, on reasonable grounds, about the financial resources they require to operate their business prudently and in compliance with the law. We expect that credit licensees will document this assessment and their conclusion, and have systems and controls to ensure that they maintain an adequate level of financial resources.
- 6 Credit licensees must also have in place adequate arrangements for compensating persons for loss or damage suffered because of breaches of the relevant obligations in the National Credit Bill by the licensee or its representatives. These arrangements must either satisfy the requirements prescribed in the regulations or be otherwise approved in writing by ASIC: see cl 48(2).
- 7 The exposure draft National Consumer Credit Protection Regulations 2009 (the draft Regulations) provide that, unless otherwise exempt, a credit licensee must hold professional indemnity insurance cover that is adequate, having regard to:
- (a) the credit licensee's membership of an approved external dispute resolution scheme or schemes, taking into account the maximum liability that has, realistically, some potential to arise in connection with:
 - (i) any particular claim against the credit licensee; and
 - (ii) all claims in respect of which the credit licensee could be found to have liability; and

- (b) relevant considerations in relation to the regulated credit business carried on by the licensee, including:
 - (i) the volume of the credit licensee's business;
 - (ii) the number and kind of clients;
 - (iii) the kind or kinds of credit activities; and
 - (iv) the number of representatives of the credit licensee (see draft reg 2.5)

Note: The draft Regulations were published by Treasury on 27 April 2009.

- 8 When considering alternative arrangements, in addition to the adequacy measures in draft reg 2.5, ASIC must have regard to the credit activities carried on under the licence of the licensee and whether the arrangements will be sufficient to cover consumers after the licensee ceases to engage in credit activities and for how long: see cl 48(3)(b). This is discussed further in Section D.
- 9 Draft reg 2.5 exempts from the compensation requirements general insurance companies, life insurance companies and ADIs regulated by APRA. It also includes companies that have an ASIC-approved guarantee from a related APRA-regulated entity.

Relationship with compensation and financial resources requirements for AFS licensees

Financial resources

- 10 In developing the proposals in this paper, we have drawn on our experience in administering the financial requirements we currently impose on an AFS licensee under Regulatory Guide 166 *Licensing: Financial requirements* (RG 166). Both regimes are concerned with ensuring that a licensee has adequate financial resources to engage in the activities authorised by its licence and to carry out supervisory arrangements. However, the activities authorised by an Australian financial services (AFS) licence are quite different from the credit activities authorised by an Australian credit licence (credit licence).
- 11 An AFS licensee provides financial services in relation to investment or risk management products or payment facilities—these products involve the client spending their own money. By contrast, a lender of credit provides its own money to the consumer. This means that consumer protection considerations do not require the same high level of financial resources for a credit licensee. For this reason, we propose that credit licensees self-assess whether they have adequate financial resources: see proposal B1.

Compensation

- 12 In developing the proposals in this paper, we have also drawn on our experience in administering the professional indemnity (PI) insurance requirements for AFS licensees under Regulatory Guide 126 *Compensation and insurance arrangements for AFS licensees* (RG 126). As a result, the proposed compensation arrangements outlined in this paper are similar to the features of PI insurance that characterise the regime for AFS licensees.
- 13 The key distinction between the requirements in RG 126 and the compensation arrangements for credit licensees is that for lenders there will be no specific minimum *amount* of PI insurance cover they must hold. Instead, lenders will be expected to:
- (a) analyse the circumstances in which their credit activities could expose them to an obligation to compensate a consumer beyond merely reducing the size of the consumer's loan; and
 - (b) obtain PI insurance cover sufficient to meet that exposure.
- 14 This proposal includes lenders who also provide some credit assistance because the provision of assistance will generally be ancillary to the primary activity of providing credit. This means that where a lender also provides credit assistance, they should consider the risks associated with that part of their credit activities when determining how much PI insurance cover is required for their business.
- 15 Those elements of RG 126 that we propose to carry across for credit licensees are:
- (a) the key features of an adequate PI insurance policy;
 - (b) for non-lenders (that do not otherwise provide credit), the requirement to hold a minimum amount of PI insurance cover; and
 - (c) the approach to the alternative arrangements regime, where credit licensees can apply to ASIC for approval of a non-PI insurance based compensation arrangement.
- 16 We recognise that consumer protection considerations associated with the businesses of credit licensees are quite different from those applicable to AFS licensees. Some of the questions we ask in this paper are directed to exploring the ramifications of those differences.

What are the requirements designed to achieve?

- 17 The legislative financial resources requirements are designed to help ensure that credit licensees have sufficient financial resources to conduct their business in compliance with the National Credit Bill and their credit licence

obligations (including carrying out supervisory arrangements). They are not intended to ensure that credit licensees will always be able to meet their financial commitments (including commitments to consumers).

18 In any industry, from time to time, clients might suffer loss due to inappropriate advice or other misconduct by a service provider. In the credit industry, compensation arrangements are a mechanism to ensure that funds are likely to be available where consumers suffer losses that result from poor quality services and other misconduct by a credit licensee.

19 The overarching objective of compensation requirements is to reduce the risk that losses sustained by consumers cannot be compensated by the credit licensee because of a lack of available financial resources.

20 The proposed compensation requirements are designed to reduce this risk of uncompensated consumer losses. They are not, however, meant to be a mechanism for providing compensation directly to consumers and may not cover all possible consumer losses.

21 The following basic policy principles will guide the administration of the financial resources and compensation requirements for credit licensees:

- (a) we expect credit licensees will be able to demonstrate to us why they think they have adequate resources when applying for a licence and at all times thereafter;
- (b) the primary way for credit licensees to comply with the compensation requirements will be to hold adequate professional indemnity insurance; and

Note: Clause 47(2) of the National Credit Bill states that when considering whether an arrangement is adequate ASIC must take into account the nature, scale and complexity of the credit activities engaged in by the credit licensee.

- (c) the standard of adequate PI insurance cover will be the benchmark for ASIC approval of any alternative compensation arrangements proposed by credit licensees.

B Adequate financial resources

Key points

We propose that credit licensees (other than those that are also APRA-regulated):

- self-assess whether they have adequate financial resources to conduct their business in compliance with the National Credit Bill and their credit licence obligations: see proposal B1; and
- confirm to ASIC annually that they have sufficient financial resources to conduct their business in compliance with the National Credit Bill and their credit licence obligations and to meet their obligations as they fall due in the near future (generally this should cover at least the next three months): see proposal B2.

Underlying principles

- 22 The proposals in this section (Section B) are designed to enhance consumer protection and market integrity by ensuring that credit licensees have sufficient financial resources to conduct their business in compliance with the National Credit Bill (including carrying out supervisory arrangements). While it is important that credit licensees meet their financial commitments (including commitments to consumers), the high-level financial resource requirements are not designed to guarantee that this takes place.
- 23 The National Credit Bill states that, among other obligations, a credit licensee must:
- (a) have available adequate financial resources to provide the financial services covered by the credit licence and to carry out supervisory arrangements (see cl 47(1)(i));
 - (b) do all things necessary to ensure that the activities covered by the credit licence are provided efficiently, honestly and fairly (see cl 47(1)(a));
 - (c) have adequate risk management systems (see cl 47(1)(ii)); and
 - (d) comply with the conditions on their licence (see cls 47(1)(c) and 47(1)(m)), including the prescribed conditions under draft regulation 2.2 (draft reg 2.2).
- 24 The legislation's aim in imposing financial resources requirements is to help ensure that insufficient financial resources do not put compliance with the National Credit Bill and a credit licensee's licence obligations at risk. It is not our intention to impose requirements that prevent a credit licensee's

failure, but to help ensure that insufficient financial resources do not put compliance with their licence obligations at risk.

- 25 While we are not proposing to impose detailed financial requirements by way of licence conditions, our expectation is that:
- (a) 'adequate financial resources' includes access to enough financial resources to meet their obligations as they fall due in the near future (generally this should cover at least the next three months); and
 - (b) the credit licensee will document how it ensures their resources are adequate.

The requirements

- 26 Although we are not proposing to impose minimum financial resource requirements through licence conditions, we expect credit licenses to monitor their financial position on an ongoing basis. Generally, we expect this will include monitoring their cash flows and ensuring they will have adequate funds to meet their obligations as they fall due in the near future (generally this should cover at least the next three months).
- 27 We will ask for some financial information from applicants for a credit licence. We will ask further questions and request supporting documents where we think it appropriate to ask more closely as to whether an applicant is likely to have adequate financial resources to conduct their business in compliance with the National Credit Bill and their credit licence obligations.
- 28 While credit licensees must themselves take responsibility for determining what constitutes adequate financial resources in the context of their credit activities and how best to monitor their financial resources, we expect that credit licensees will:
- (a) ensure that a senior person is accountable for ensuring that their financial resources remain adequate at all times;
 - (b) ensure they have access to enough financial resources to meet their obligations as they fall due in the near future (including via overdrafts, guarantees or other funding arrangements); and
 - (c) keep written records that demonstrate that financial resources are being monitored on a regular basis.
- 29 We may also ask credit licensees from time to time to explain their assessment of their current financial resource needs and to demonstrate that they have at least that level of financial resources.

Proposal

- B1** We propose that a credit licensee (other than a licensee that is also APRA-regulated) self-assess whether it has adequate financial resources to comply with its credit licence obligations.

Your feedback

- B1Q1 Do you agree with proposal B1? Please give reasons for your views.
- B1Q2 Do you think that proposal B1 gives adequate assurance that we will achieve our objectives identified at paragraph 22? Please give reasons for your views.

- B2** We expect credit licensees to monitor their cash flows on an ongoing basis and have reasonable grounds to believe that they will have sufficient funds to meet their obligations as they fall due in the near future (generally this should cover at least the next three months).

Your feedback

- B2Q1 Do you think that proposal B2 gives adequate assurance that credit licensees will have sufficient minimum liquidity? Please give reasons for your views.
- B2Q2 Do you think that ASIC should set minimum financial requirements that apply to all credit licensees such as a base level solvency and/or a net tangible asset requirement? For example, will competitive pressure to hold less liquidity mean that credit licensees will not maintain sufficient levels of capital and liquid assets? Would imposing a base level requirement amount to an unreasonable burden?
- B2Q3 Do you think that ASIC should provide additional guidance to credit licensees about what might be considered 'adequate' financial resources?

Rationale

- 30 A credit licensee can only conduct its business in compliance with the National Credit Bill and its licence obligations if it has adequate resources, including financial resources, to do so. A credit licensee must have adequate financial resources to cover any risks the business faces that may affect its cash position or solvency and that it is reasonable for the licensee to plan to manage. If cash flow is properly planned it is less likely that a credit licensee will feel pressured to cut costs on compliance arrangements or engage in non-complying behaviour.
- 31 We believe that a credit licensee should be able to determine for itself what is adequate for its credit activities rather than being subject to ASIC-imposed minimum financial requirements. This view recognises that where the consumer is borrowing money (rather than, for example, investing or

insuring against risk), the financial standing of the counterparty (licensee) is less critical. As a result, we believe that it is not necessary to impose minimum financial requirements on all credit licensees regardless of their size and the nature of their business.

32 Moreover, we believe that our proposed approach will avoid the risk of credit licensees being discouraged from assessing and mitigating their own financial resources risk because the minimum requirements appear to take them straight to the ‘answer’. Consumers may also interpret minimum financial resources requirements as an assurance as to risk, or as ASIC endorsing the business as creditworthy.

33 To assist credit licensees with their determination of what constitutes adequate financial resources, we have provided some guidance as to our expectations. These proposals also provide high-level guidance as to the process that credit licensees should adopt to determine what constitutes adequate financial resources and the documentation of the outcomes of that process. The depth and complexity of the process will, of course, vary depending on the nature, scale and complexity of the credit licensee.

Ongoing assessment process

Proposal

- B3** We propose that a credit licensee (other than a licensee that is also APRA-regulated) will be required to confirm to ASIC annually that it:
- (a) has sufficient financial resources to comply with its licence obligations; and
 - (b) is able to meet any debts as and when they become due and payable.

Your feedback

B3Q1 Do you agree with our proposal regarding the ongoing assessment process? If not, why not? For example, does this proposal give adequate assurance that a licensee will comply with our financial requirements?

B3Q2 Do you think that we should require credit licensees to provide an annual audit report about compliance with our financial requirements? What would be the additional cost of imposing an audit requirement and would this amount to an unreasonable burden?

Rationale

34 In order to demonstrate compliance with the requirements outlined in the National Credit Bill, we believe that credit licensees (other than those that

are also APRA-regulated) should be able to demonstrate to us why they think they have adequate resources when applying for a licence and at all times thereafter.

- 35 We note the possible additional burden of requiring a credit licensee to provide a statement about compliance with the obligation to maintain adequate financial resources. However, we believe that it is necessary that we receive assurance that a credit licensee is complying with its financial requirements on an ongoing basis.
- 36 It is good business practice for credit licensees to review their financial resources regularly to ensure they continue to be adequate. Credit licensees should review the adequacy of their financial resources in light of any major changes in their business (e.g. if they start providing new services or products or engage more representatives).

Licence conditions

- 37 In light of the above, we may develop a licence condition for credit licensees (other than those that are also APRA-regulated) confirming that they need to certify to us in writing annually that they have adequate financial resources. Alternatively, this confirmation may form part of the annual compliance certificate: see cl 53 and draft reg 2.2(14). At this stage, we expect the certification to follow a simple standardised form.

C Adequate professional indemnity insurance

Key points

Whether a PI insurance policy for credit licensees (other than those that are also APRA-regulated) is adequate depends on three factors:

- the amount of the cover (see proposals C1–C3);
- the scope of the cover (see proposal C4); and
- whether the terms and conditions of the cover undermine the overall effect (e.g. by excluding cover for key aspects of the credit licensee’s business).

Our proposals expand on each of these factors in more detail.

- 38 A credit licensee’s PI insurance cover will be adequate if it maximises the potential to reduce the risk that a consumer’s losses cannot be compensated by a credit licensee. This section of the paper outlines our proposals on what we consider to be an adequate PI insurance policy.

Note: To ensure consistent requirements for all credit licensees, we will assess any applications for alternative compensation arrangements against the benchmark of adequate PI insurance cover.

- 39 Whether a particular PI insurance policy is adequate for a credit licensee depends on all of the facts and circumstances of each individual credit licensee, including the nature, scale and complexity of the licensee’s business and its other financial resources: see Section B.

Amount of cover

- 40 If a PI insurance policy is going to be an effective mechanism for compensating consumer losses, the amount of cover provided must be sufficient. In this context, this means both:
- (a) the ‘per claim’ limit of liability—that is, the maximum insurance cover for *each* individual claim; and
 - (b) the ‘in the aggregate’ limit of liability—that is, the maximum insurance cover for *all* claims.
- 41 What is an adequate PI insurance policy will differ between individual licensees, and between lenders and non-lenders. More specifically, the National Credit Bill requires ASIC to consider adequacy according to:
- (a) the extent of the credit activities undertaken by the credit licensee, including the scale of activities undertaken by credit representatives;

- (b) the nature of its business; and
- (c) the likelihood of claims against that credit licensee (see cl 47(2)).

Proposal

c1 We propose that:

- (a) the appropriate measure of a credit licensee's size is the total gross revenue derived from its credit activities that involve dealings with consumers;
- (b) for **non-lenders**, the minimum cover should be assessed on a sliding scale as follows:
 - (i) a set minimum (e.g. we are seeking your views as to whether \$2 million cover or another amount is appropriate); and
 - (ii) cover should be approximately equivalent to actual or expected revenue from retail credit activities (up to a capped maximum of \$20 million cover);
- (c) for **lenders**, we do not propose to specify a minimum amount of cover. Instead, the lender must self-assess the amount of PI insurance cover needed for their business, taking into account any assistance they might provide to consumers and the risks that may arise from such activities.

Your feedback

- C1Q1 Do you agree with our proposals on what is an adequate amount of cover?
- C1Q2 Should ASIC distinguish between lenders and non-lenders as outlined in the proposal? Please give reasons for your views.
- C1Q3 Do you believe that \$2 million is an appropriate minimum level of PI insurance cover for credit licensees (as currently applies to AFS licensees)? Or do you think that different risk considerations apply and a lower limit of \$1 million is appropriate (as currently applies to finance brokers licensed in Western Australia)?

- ### c2 We are considering how to best define 'lenders' and 'non-lenders' for the purposes of compensation requirements. Our proposals are either:
- (a) a straightforward test—that is, licensees who provide credit (whether or not they also conduct any other credit activities) would be considered lenders for the purposes of proposal C1, and all others would be regarded as non-lenders; or
 - (b) a 'primary business test'—that is, licensees whose primary business is providing credit would be considered lenders for the purposes of proposal C1, and all others would be regarded as non-lenders.

Your feedback

- C2Q1 Which definition of 'lender'/'non-lender' do you prefer and why?

C2Q2 Do you think the description of the 'primary business' test is sufficiently clear for you to apply it to your activities? If not, what additional detail do you suggest?

Rationale

42 Preliminary discussions with industry representatives indicate that the minimum requirements for the amount of cover employed under RG 126 appear to be a good way to measure credit licensee 'size' for these purposes, and provide a sensible basis for determining the minimum aggregate cover an individual credit licensee should hold. That said, we invite suggestions for alternative way of determining the correct amount of cover for credit licensees.

43 Our experience in administering RG 126 suggests that a sliding scale approach to determining the amount of adequate cover is appropriate to take account of the different business models that credit licensees might adopt. In particular, our experience suggests that smaller entities need minimum cover of at least \$1 million or possibly \$2 million in aggregate, with larger entities needing a larger amount.

44 We are aware that finance brokers currently licensed under the Western Australian regime are subject to existing PI insurance requirements. Further, Mortgage & Finance Association of Australia (MFAA) members are required (via their membership) to hold PI insurance of a minimum of \$1 million for any one claim and \$2 million in the aggregate.

45 For lenders, any consumer compensation might be able to be offset against the size of the consumer's loan or lease and this makes PI insurance less critical as a compensation mechanism. This will often be the case even if the consumer's complaint arises from the lender's provision of credit assistance rather than the provision of credit. For this reason, we are not proposing to require lenders to hold a specific *amount* of PI insurance. Instead, we expect lenders to:

- (a) analyse the circumstances in which their engagement in credit activities could expose them to an obligation to compensate consumers in a way other than by reducing the consumer's loan or lease; and
- (b) obtain PI insurance cover that is adequate to meet this potential exposure.

Note: Both lenders and non-lenders are required to hold 'adequate' PI insurance under the National Credit Bill and draft regulations.

Scope of cover

- 46 Clause 48(1) requires that the compensation arrangements cover loss or damage suffered because of a contravention of an obligation under the National Credit Bill by the credit licensee or its representatives.
- 47 Credit licensees will be subject to broad obligations under the National Credit Bill when it becomes law, including a duty do all things necessary to ensure that the credit activities authorised by the licence are engaged in efficiently, honestly and fairly. Losses caused by negligent, fraudulent or dishonest conduct that amounts to a breach of the National Credit Bill should be covered.

Proposal

- c3** In light of the National Credit Bill and draft Regulations and the objective of the compensation arrangements, we propose the following as key features of an adequate PI insurance policy:
- (a) it must cover loss or damage suffered by consumers because of breaches of obligations under the National Credit Bill or licence obligations;
 - (b) it must cover breaches by both the credit licensee and its representatives;
 - (c) it must be available to cover compensation awards made by the EDR scheme(s) to which the credit licensee and its representatives belongs; and
 - (d) as far as possible, it must continue to provide access for potential claims that come to light after either the policy expires or the credit licensee ceases business for a reasonable period (e.g. run-off cover or an extended reporting period).

Your feedback

C3Q1 Do you agree with our proposal on what is an adequate *scope of cover*? Please give reasons.

C3Q2 Do you agree with our proposal that an adequate policy must continue to provide access for potential claims for a reasonable period after the policy expires or the credit licensee ceases business? Please give reasons.

- 48 Our experience in administering RG 126 suggests policies with run-off cover or an extended reporting period are not always readily available for all licensees: see proposal C3(d). However, we expect licensees to take reasonable steps to obtain cover with this feature.

Exclusions, excesses and deductibles

Exclusions

- 49 Exclusions in a PI insurance policy that impact on the credit licensee's ability to compensate consumer losses will ordinarily make that policy inadequate, especially exclusions that relate directly to the minimum scope of cover outlined above. For example, exclusions relating to breaches of the National Credit Bill and the regulations would be considered as not meeting the purpose of the compensation requirements.
- 50 More specifically, we consider exclusions dealing with the following to be significant:
- (a) EDR scheme awards and awards made by the Federal Court under the proposed small claims (i.e. up to \$40,000) jurisdiction;
 - (b) loss caused by the conduct of representatives;
 - (c) fraud and dishonesty by agents and representatives; and
 - (d) claims for misrepresentations about services.

Excesses and deductibles

- 51 Excesses and deductibles are common features of PI insurance policies currently in the market; a high excess or deductible might have the effect of the credit licensee having to draw heavily on their financial resources before being able to draw on the policy to meet a consumer's claim for compensation. Credit licensees should ensure that they are able to cover excesses out of their own funds otherwise their PI policy is unlikely to be adequate.

Who can provide the cover?

- 52 Our experience in administering RG 126 shows how important it is that licensees hold PI insurance cover only from financially sound and well regulated insurers. As such, we believe that only APRA-regulated general insurers and certain exempt foreign insurers are able to provide adequate cover. This does not prevent credit licensees from seeking ASIC approval of alternative arrangements from bodies other than these. Such arrangements are discussed further in Section D.

Proposal

- c4** We propose that PI insurance cover must be provided by an insurer regulated by APRA under the *Insurance Act 1973* or exempted under that Act.

Note: See Section D for our proposals about alternative arrangements.

Your feedback

- C4Q1 Should anyone other than an APRA-regulated insurer or limited direct offshore foreign insurers be able to provide PI insurance cover for the purposes of the compensation requirements for credit licensees? Please give reasons.

Process for obtaining cover

- 53 Notwithstanding the PI insurance requirements proposed in this paper, credit licensees should undertake their own analysis of what is adequate PI insurance cover for them. Some credit licensees might find it helpful to engage external consultants, actuaries, brokers or advisers to undertake a risk assessment of their business and provide advice on the amount and type of cover that they should obtain.
- 54 Whether or not a credit licensee already has PI insurance cover in place upon the commencement of the legislation, ASIC will not formally ‘approve’ a credit licensee’s PI insurance arrangements.

Initial assessment process

- 55 Under draft reg 2.5, a credit licensee must determine whether its PI insurance cover is adequate having regard to:
- (a) its membership of an external dispute resolution (EDR) scheme or schemes (including those schemes of which its credit representatives are members), taking account of the maximum liability that has, realistically, some potential to arise in connection with any particular claim against the licensee and all claims in respect of which the licensee could be found to be liable; and
 - (b) relevant considerations of the credit activities carried out by the licensee, including:
 - (i) the volume of business;
 - (ii) the number and kind of clients;
 - (iii) the kind or kinds of business; and
 - (iv) the number of representatives.

56 The list of factors in draft reg 2.5 is not an exhaustive list of the factors credit licensees need to take into account in assessing what PI insurance cover is adequate in their circumstances. Terms of the insurance policy itself are also vital in determining whether the cover complies with the obligations under cl 48 and draft reg 2.5.

Proposal

c5 We propose that credit licensees go through the process outlined in Table 1 to determine what will be adequate PI insurance for them. Table 2 lists key questions we propose credit licensees ask when determining whether a particular policy is adequate.

Your feedback

- C5Q1 Are the steps in Table 1 and questions in Table 2 helpful for licensees to consider in assessing what is adequate cover? Are there any other processes or procedures that you follow when obtaining and maintaining PI insurance that ASIC should discuss in its policy?
- C5Q2 Is the guidance in this section of the paper likely to directly result in any increase in your compliance costs? Please give details, including figures and reasons.

Table 1: Initial assessment process

Step 1	Assess the business: including claims history, level of business and risk management procedures (including proposed changes to the business)
Step 2	Assess potential liability: we suggest that credit licensees can determine 'the maximum liability that has, realistically, some potential to arise' under draft reg 2.5 by making a reasonable estimate of the following factors: <ul style="list-style-type: none"> • the maximum exposure to a single client ('worst case scenario'); • the number of claims that could arise from a single event (potential for multiple claims); and • the number of claims that might be expected during the policy period.
Step 3	Ask insurers or insurance brokers for a list of key policy features, exclusions and available extensions (based on full disclosure of the information the licensee has assembled under Steps 1 and 2).
Step 4	Consider whether the amount and scope of cover is adequate in light of the features identified in Section C of this paper.
Step 5	Review the policy by asking a series of questions (outlined in Table 2) as to the adequacy of the cover.

Table 2: Key questions for credit licensees

Policy features	Questions to ask
Scope of cover and extensions	<p>Does the policy cover:</p> <ul style="list-style-type: none"> • losses from breaches of the National Credit Bill by the credit licensee and its representatives? • negligence and other common law claims generally? • fraud and dishonest conduct by agents and representatives? • EDR scheme awards relating both to the credit licensee and all of its representatives? Does it cover agreed decisions reached through the EDR scheme conciliation process?
Amount of cover	<p>Does the policy have an adequate level of indemnity to cover a reasonable estimate of consumer losses?</p> <p>Is the level of indemnity adequate to cover claims brought both inside and outside EDR schemes?</p> <p>Does the level of indemnity cover claims relating to losses for which a credit licence is not required? This is important as these claims can reduce the amount of cover available for claims that are made by consumers, meaning the licensee might need to increase the level of cover to take account of this. Are defence costs covered separately from the amount of indemnity cover?</p> <p>Does the policy provide for automatic reinstatement? This means that if the limit of the policy is exhausted before the end of the policy period, the credit licensee can pay a new premium so that the limit of indemnity is reinstated for the balance of the period to cover any new claims that might arise before the policy is renewed.</p> <p>Does the business carry a higher risk of claims or is it exposed to a higher volume of claims and therefore requires a larger amount of PI insurance cover?</p> <p>Have weaknesses been identified in your compliance systems, such as a high number of claims or high-risk products/practices, which might mean a higher level of cover is required?</p>
Excess/ deductibles	Is the excess at a level that the business can confidently sustain as an uninsured loss taking into account the credit licensee's financial resources?
Exclusions	What are the exclusions from cover? Are the exclusions significant? Does the credit licensee have sufficient financial resources to cover these exclusions?
Approved product list	Is cover limited to services provided in relation to an agreed list of products?
Who is covered?	<p>Does the policy cover the credit licensee and all of its representatives? This can be under the primary policy or under a separate policy under which the credit licensee has a right of indemnity.</p> <p>Are there many representatives and are they geographically dispersed? If so, the limit of indemnity might need to be appropriately higher to manage this risk.</p>
Retroactive cover	If the credit licensee had a previous PI insurance policy prior to being licensed, does the new policy provide retroactive cover from the date of expiration of the previous policy?
'Run-off' cover	Does the policy provide run-off cover or an extended reporting period? If so, for how long?

Ongoing assessment process

- 57 We expect that credit licensees will review their PI insurance or other compensation arrangements at least annually to ensure they continue to be adequate (e.g. when the existing policy is up for renewal). Credit licensees should also review the adequacy of their compensation arrangements in light of any major changes in their business (e.g. if they start providing new services or products or engage more representatives).

Compliance systems

- 58 We expect credit licensees will ensure that a senior person is accountable for ensuring that their PI insurance policy is renewed when required, that premiums are paid on time and that their policy or other compensation arrangements continue to be adequate. Credit licensees will need to make provision in their internal dispute resolution systems for ensuring that claims that are brought to their attention are promptly notified to insurers.

Licence conditions

- 59 We may develop a licence condition for credit licensees (other than those that are also APRA-regulated) confirming that they need to obtain PI insurance that is adequate in terms of its amount, scope, and other terms and conditions.

New licensees

- 60 Applicants for a credit licence will need to confirm in their application that they have:
- (a) adequate compensation arrangements in place; or
 - (b) a process to ensure that they will have adequate compensation arrangements in place when their credit licence takes effect.

Proposal

- c6** We propose to ask applicants for a credit licence questions about:
- (a) the insurer and the type and level of PI insurance cover they have in place;
 - (b) the scope of cover and whether the policy covers claims relating to all the products that the credit licensee wishes to provide under the licence; and
 - (c) whether the PI insurance policy contains the important policy features that are outlined in Section C of this paper.

Your feedback

C6Q1 Are there any practical problems with requesting this information?

D Alternative arrangements and exemptions

Key points

Credit licensees wishing to apply for ASIC approval of alternative compensation arrangements under cl 48(2) will need to lodge an application for approval.

Applications for approval of alternative arrangements will be assessed on a case-by-case basis.

Some APRA-regulated entities that are also credit licensees are to be exempt from the requirement to hold PI insurance.

Subsidiaries of some APRA-regulated entities that are also credit licensees may also be exempt from the requirement to hold PI insurance where they have an ASIC-approved guarantee from the APRA-regulated entity.

Our proposals about how we will assess these applications are discussed in this section.

Applying for approval of alternative arrangements

- 61 We propose that credit licence applicants will be asked on their licence application whether they are going to seek ASIC approval for compensation arrangements other than PI insurance. Applicants should apply for approval of their alternative arrangements as part of their licence application process. Some examples of hypothetical alternative arrangements are provided at Table 3. These are examples only and we propose assessing applications for alternative arrangements on a case-by-case basis. By including these examples in the table, we make no statement as to whether arrangements of this kind would always constitute ‘adequate’ compensation arrangements or would be approved by ASIC in any particular circumstance or for any given credit licensee.
- 62 This approach mirrors that applied under RG 126 for AFS licensees seeking to use alternative arrangements instead of holding adequate PI insurance cover. We believe that this process has merit in light of our experience in administering RG 126 to date.
- 63 We propose that an application for ASIC approval of alternative compensation arrangements should address the following issues:
- (a) whether more than one credit licensee will be covered by the arrangements and, if so, who they are. This will apply where the

arrangements over a group of related credit licensees or an industry sector or other sub-group of licensees;

- (b) how the arrangements meet the criteria for assessing adequate PI insurance (see Section C);
- (c) any benefits, risks or costs to consumers arising from the credit licensees using these arrangements rather than PI insurance; and
- (d) any circumstances particular to the credit licensee or the industry sector which make these arrangements more appropriate than PI insurance.

64 We will assess each application on its merits. We will give priority to group applications, for example, where they apply to an industry sector or sub-sector.

65 Should a credit licensee with high levels of financial resources wish to ‘self-insure’ (i.e. cover the cost of claims using their own available financial resources), we will assess these arrangements using the same process as for other arrangements.

Table 3: Examples of hypothetical alternative arrangements (subject to case-by-case approval)

Industry member fund	<p>Alternative arrangements proposed by an industry body may be approved by ASIC. For example, an industry body’s members might wish to set up a compensation fund supported by compulsory levies of members.</p> <p>This could be in addition to PI insurance (i.e. to compensate clients where a member’s insurance is inadequate or they cease trading or become insolvent) or instead of PI insurance. Approval of a fund would depend on the amount of compensation that would be available for clients and the circumstances in which the fund would compensate clients.</p> <p>We encourage industry bodies to consider whether an alternative arrangement is appropriate for their members and we are keen to discuss any such arrangements further with them.</p>
Self-insurance	<p>Some very highly capitalised credit licensees might take a self-insurance approach (i.e. to completely replace PI insurance). This might be appropriate for credit licensees that are so substantial that failure to pay claims is very unlikely. This is akin to the exemption proposed for some APRA-regulated entities.</p> <p>We think that only credit licensees that are very highly capitalised will find this an adequate alternative to PI insurance cover.</p>
Discretionary mutual fund	<p>Discretionary mutual funds (DMFs) are entities that offer ‘discretionary cover’—that is, an insurance-like product that may involve an obligation on the DMF to consider meeting a claim made on it, but gives the DMF a discretion as to whether it will pay the claim. A DMF may be a trust, mutual, company limited by guarantee or other structure.</p>

Security bond

A security bond is a performance bond issued by:

- an Australian authorised-deposit taking institution authorised under the *Banking Act 1959*;
- a general insurance company authorised under the *Insurance Act 1973*; or
- a state government insurance office,

where the purpose of the deposit is to compensate clients who have suffered a pecuniary loss due to the failure of the credit licensee to carry on its credit activities adequately and properly.

- 66 Our policy on relief applications is set out in Regulatory Guide 51 *Applications for relief* (RG 51). In addition to this policy, we will also consider the intention behind the introduction of cl 48, which is that all credit licensees have arrangements to minimise the risk that consumer losses cannot be compensated. On this basis, it is unlikely that we would grant relief from the requirements in cl 48 and draft reg 2.5.

Assessment criteria for applications

- 67 Under draft reg 2.5, when deciding whether to approve alternative compensation arrangements, we will be required to have regard to:
- (a) the nature of the credit activities undertaken; and
 - (b) whether the arrangements provide cover after the credit licensee ceases the business and, if so, for how long.
- 68 The regulation also explicitly requires us to take into account the factors we use to assess adequacy of PI insurance when approving alternative arrangements. This means that alternative arrangements must also be adequate having regard to:
- (a) the credit licensee's membership of an EDR scheme (including the schemes of which the licensee's credit representatives are members) or schemes taking into account the maximum liability that has, realistically, some potential to arise;
 - (b) the volume of business;
 - (c) the number and kind of clients;
 - (d) the kind or kinds of business; and
 - (e) the number of representatives.
- 69 When individual credit licensees ask us to approve alternative arrangements, we propose that they follow the steps outlined in Table 2 and to share the outcome of their calculations with us. This is to help us evaluate whether the alternative arrangements are adequate. If the credit licensee is unable to demonstrate that its proposed alternative arrangement can confidently cover

the estimated exposure (as confirmed by an external expert, such as an auditor or an actuary), the arrangement is unlikely to be approved by ASIC.

- 70 When a lender approaches us seeking approval of an alternative arrangement, we will consider whether any proposals put to us will achieve the legislative objective of compensating losses of consumers on their merits.

Proposal

- D1 We propose to assess applications for alternative arrangements by comparing them to PI insurance arrangements to ensure that credit licensees and their clients have comparable protection where alternative arrangements are used in lieu of PI insurance.
- (a) For non-lenders, we propose to approve alternative arrangements only where they provide no less protection than adequate PI insurance cover.
 - (b) For lenders, we will consider each proposed alternative arrangement on its merits and against the compensation needs of the credit activities of that licensee.

Your feedback

- D1Q1 Do you agree with our approach to assessing alternative arrangements? Please give reasons.
- D1Q2 Are there other alternative arrangements you might consider using in place of PI insurance cover? Please provide details.

Licensees exempt under the Regulations

- 71 The draft regulations provide that certain credit licensees will be exempt from the compensation requirements. This applies to general insurance companies, life insurance companies and ADIs regulated by APRA that also undertake credit activities.

APRA-regulated institution provided guarantees

- 72 Credit licensees that are related to any APRA-regulated institution (i.e. ADIs, general insurance companies and life insurance companies) are also exempt where they have a guarantee by the APRA-regulated institution that has been approved by ASIC.

Proposal

- D2 We propose to approve guarantees only where they provide no less protection than adequate PI insurance cover: see draft reg 2.5.

Your feedback

D2Q1 Do you agree with our proposal on approved guarantees? Please give reasons.

D2Q2 We understand that APRA may treat such guarantees as a form of capital support. Taking this into consideration, to what extent do you think that this exemption is likely to be used?

Rationale

- 73 In considering whether to approve a guarantee of this nature, we will consider the same factors outlined in Section C in relation to the adequacy of PI insurance. APRA-regulated entities are permitted to give guarantees that are limited in time and amount and we have no in-principle objection to such limits in guarantees put to us for approval (assuming, of course, that the limits are appropriate in the circumstances).

E Regulatory and financial impact

74 In developing the proposals in this paper, we have carefully considered their regulatory and financial impact. On the information currently available to us we think they will strike an appropriate balance between:

- (a) ensuring that consumers of credit licensees have access to adequate compensation mechanisms; and
- (b) not causing credit licensees to incur unreasonable costs in setting their financial resources and obtaining PI insurance cover.

75 Before settling on a final policy, we will comply with the requirements of the Office of Best Practice Regulation (OBPR) by:

- (a) considering all feasible options;
- (b) if regulatory options are under consideration, undertaking a preliminary assessment of the impacts of the options on business and individuals or the economy;
- (c) if our proposed option has more than low impact on business and individuals or the economy, consulting with OBPR to determine the appropriate level of regulatory analysis; and
- (d) conducting the appropriate level of regulatory analysis—that is, complete a Business Cost Calculator report (BCC report) and/or a Regulation Impact Statement (RIS).

76 All BCC reports and RISs are submitted to the OBPR for approval before we make any final decision. Without an approved BCC report and/or RIS, ASIC is unable to give relief or make any other form of regulation, including issuing a regulatory guide that contains regulation.

77 To ensure that we are in a position to properly complete any required BCC report or RIS, we ask you to provide us with as much information as you can about:

- (a) the likely compliance costs;
- (b) the likely effect on competition; and
- (c) other impacts, costs and benefits,

of our proposals or any alternative approaches: see ‘The consultation process’, p. 4.

Key terms

Term	Meaning in this document
ADI	An authorised deposit-taking institution as defined under the <i>Banking Act 1959</i>
AFS licence	An Australian financial services licence under s913B of the <i>Corporations Act 2001</i> that authorises a person who carries out a financial services business to provide financial services <p>Note: This is a definition contained in s761A of the <i>Corporations Act 2001</i>.</p>
APRA	Australian Prudential Regulation Authority
credit licence	An Australian credit licence under cl 35 of the National Credit Bill that authorises a licensee to engage in particular credit activities
lender	A credit provider as defined in s204 of the National Credit Code
National Credit Bill	National Consumer Credit Protection Bill 2009 as tabled on 25 June 2009
non-lender	All credit licensees that are not lenders. This category includes persons who provide credit assistance under cl 9 of the National Credit Bill and persons who act as intermediaries under cl 8 of the National Credit Bill
PI insurance	Professional indemnity insurance

List of proposals and questions

Proposal	Your feedback	
B1 We propose that a credit licensee (other than a licensee that is also APRA-regulated) self-assess whether it has adequate financial resources to comply with its credit licence obligations.	B1Q1	Do you agree with proposal B1? Please give reasons for your views.
	B1Q2	Do you think that proposal B1 gives adequate assurance that we will achieve our objectives identified at paragraph 22? Please give reasons for your views.
B2 We expect credit licensees to monitor their cash flows on an ongoing basis and have reasonable grounds to believe that they will have sufficient funds to meet their obligations as they fall due in the near future (generally this should cover at least the next three months).	B2Q1	Do you think that proposal B2 gives adequate assurance that credit licensees will have sufficient minimum liquidity? Please give reasons for your views.
	B2Q2	Do you think that ASIC should set minimum financial requirements that apply to all credit licensees such as a base level solvency and/or a net tangible asset requirement? For example, will competitive pressure to hold less liquidity mean that credit licensees will not maintain sufficient levels of capital and liquid assets? Would imposing a base level requirement amount to an unreasonable burden?
	B2Q3	Do you think that ASIC should provide additional guidance to credit licensees about what might be considered 'adequate' financial resources?
B3 We propose that a credit licensee (other than a licensee that is also APRA-regulated) will be required to confirm to ASIC annually that it: <ul style="list-style-type: none"> (a) has sufficient financial resources to comply with its licence obligations; and (b) is able to meet any debts as and when they become due and payable. 	B3Q1	Do you agree with our proposal regarding the ongoing assessment process? If not, why not? For example, does this proposal give adequate assurance that a licensee will comply with our financial requirements?
	B3Q2	Do you think that we should require credit licensees to provide an annual audit report about compliance with our financial requirements? What would be the additional cost of imposing an audit requirement and would this amount to an unreasonable burden?

Proposal	Your feedback	
<p>C1 We propose that:</p> <p>(a) the appropriate measure of a credit licensee's size is the total gross revenue derived from its credit activities that involve dealings with consumers;</p> <p>(b) for non-lenders, the minimum cover should be assessed on a sliding scale as follows:</p> <p>(i) a set minimum (e.g. we are seeking your views as to whether \$2 million cover or another amount is appropriate); and</p> <p>(ii) cover should be approximately equivalent to actual or expected revenue from retail credit activities (up to a capped maximum of \$20 million cover);</p> <p>(c) for lenders, we do not propose to specify a minimum amount of cover. Instead, the lender must self-assess the amount of PI insurance cover needed for their business, taking into account any assistance they might provide to consumers and the risks that may arise from such activities.</p>	<p>C1Q1</p> <p>C1Q2</p> <p>C1Q</p>	<p>Do you agree with our proposals on what is an adequate amount of cover?</p> <p>Should ASIC distinguish between lenders and non-lenders as outlined in the proposal? Please give reasons for your views.</p> <p>Do you believe that \$2 million is an appropriate minimum level of PI insurance cover for credit licensees (as currently applies to AFS licensees)? Or do you think that different risk considerations apply and a lower limit of \$1 million is appropriate (as currently applies to finance brokers licensed in Western Australia)?</p>
<p>C2 We are considering how to best define 'lenders' and 'non-lenders' for the purposes of compensation requirements. Our proposals are either:</p> <p>(a) a straightforward test—that is, licensees who provide credit (whether or not they also conduct any other credit activities) would be considered lenders for the purposes of proposal C1, and all others would be regarded as non-lenders; or</p> <p>(b) a 'primary business test' —that is, licensees whose primary business is providing credit would be considered lenders for the purposes of proposal C1, and all others would be regarded as non-lenders.</p>	<p>C2Q1</p> <p>C2Q</p>	<p>Which definition of 'lender'/'non-lender' do you prefer and why?</p> <p>Do you think the description of the 'primary business' test is sufficiently clear for you to apply it to your activities? If not, what additional detail do you suggest?</p>

Proposal	Your feedback	
<p>C3 In light of the National Credit Bill and draft Regulations and the objective of the compensation arrangements, we propose the following as key features of an adequate PI insurance policy:</p> <ul style="list-style-type: none"> (a) it must cover loss or damage suffered by consumers because of breaches of obligations under the National Credit Bill or licence obligations; (b) it must cover breaches by both the credit licensee and its representatives; (c) it must be available to cover compensation awards made by the EDR scheme(s) to which the credit licensee and its representatives belong; and (d) as far as possible, it must continue to provide access for potential claims that come to light after either the policy expires or the credit licensee ceases business for a reasonable period (e.g. run-off cover or an extended reporting period). 	C3Q1	Do you agree with our proposal on what is an adequate <i>scope</i> of cover? Please give reasons.
	C3Q2	Do you agree with our proposal that an adequate policy must continue to provide access for potential claims for a reasonable period after the policy expires or the credit licensee ceases business? Please give reasons.
<p>C4 We propose that PI insurance cover must be provided by an insurer regulated by APRA under the <i>Insurance Act 1973</i> or exempted under that Act.</p> <p>Note: See Section D for our proposals about alternative arrangements.</p>	C4Q1	Should anyone other than an APRA-regulated insurer or limited direct offshore foreign insurers be able to provide PI insurance cover for the purposes of the compensation requirements for credit licensees? Please give reasons.
<p>C5 We propose that credit licensees go through the process outlined in Table 1 to determine what will be adequate PI insurance for them. Table 2 lists key questions we propose credit licensees ask when determining whether a particular policy is adequate.</p>	C5Q1	Are the steps in Table 1 and questions in Table 2 helpful for licensees to consider in assessing what is adequate cover? Are there any other processes or procedures that you follow when obtaining and maintaining PI insurance that ASIC should discuss in its policy?
	C5Q2	Is the guidance in this section of the paper likely to directly result in any increase in your compliance costs? Please give details, including figures and reasons.

Proposal	Your feedback	
<p>C6 We propose to ask applicants for a credit licence questions about:</p> <ul style="list-style-type: none"> (a) the insurer and the type and level of PI insurance cover they have in place; (b) the scope of cover and whether the policy covers claims relating to all the products that the credit licensee wishes to provide under the licence; and (c) whether the PI insurance policy contains the important policy features that are outlined in Section C of this paper. 	C6Q1	Are there any practical problems with requesting this information?
<p>D1 We propose to assess applications for alternative arrangements by comparing them to PI insurance arrangements to ensure that credit licensees and their clients have comparable protection where alternative arrangements are used in lieu of PI insurance.</p> <ul style="list-style-type: none"> (a) For non-lenders, we propose to approve alternative arrangements only where they provide no less protection than adequate PI insurance cover. (b) For lenders, we will consider each proposed alternative arrangement on its merits and against the compensation needs of the credit activities of that licensee. 	D1Q1	Do you agree with our approach to assessing alternative arrangements? Please give reasons.
	D1Q2	Are there other alternative arrangements you might consider using in place of PI insurance cover? Please provide details.
<p>D2 We propose to approve guarantees only where they provide no less protection than adequate PI insurance cover: see draft reg 2.5.</p>	D2Q1	Do you agree with our proposal on approved guarantees? Please give reasons?
	D2Q2	We understand that APRA may treat such guarantees as a form of capital support. Taking this into consideration, to what extent do you think that this exemption is likely to be used?