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THE PARLIAMENT OF THE COMMONWEALTH OF AUSTRALIA

HOUSE OF REPRESENTATIVES

INSURANCE CONTRACTS AMENDMENT BILL 2010

EXPLANATORY MEMORANDUM

(Circulated by authority of the Minister for Financial Services, Superannuation and
Corporate Law, the Hon Chris Bowen MP)

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Glossary

The following abbreviations and acronyms are used throughout this explanatory memorandum.

<i>Abbreviation</i>	<i>Definition</i>
ALRC	Australian Law Reform Commission
ASIC	Australian Securities and Investments Commission
Bill	Insurance Contracts Amendment Bill 2010
ET Act	<i>Electronic Transactions Act 1999</i>
IC Act	<i>Insurance Contracts Act 1984</i>
Review Panel	The Panel appointed to review the IC Act

General outline and financial impact

Outline

1.1 The Insurance Contracts Amendment Bill 2010 (the Bill) arose out of recommendations made by a review of the *Insurance Contracts Act 1984* (the IC Act). This review was conducted by a Panel comprising Mr Alan Cameron AM and Ms Nancy Milne (the Review Panel). The Review Panel's main conclusion was that the IC Act was generally working satisfactorily to the benefit of insurers and insureds. However, the Review Panel found that some changes would be beneficial, given the passage of time since the Act was originally enacted, developments in the insurance market since that time and judicial interpretation of IC Act provisions.

1.2 The Review Panel made detailed recommendations for changes to the IC Act to address issues that had been identified as arising from the above factors. This Bill gives effect to a number of the Review Panel's recommendations. In several areas the Review Panel's recommended approach was modified to take account of subsequent consultations with stakeholders on the details of the proposed amendments.

Major elements

1.3 The following is a brief summary of the measures included in the Bill, outlined under their particular Schedule number.

Schedule 1 — Scope and application

1.4 Schedule 1 to the Bill contains amendments that relate to the scope and application of the IC Act. It amends the IC Act so that:

- failure to comply with the duty of utmost good faith is a breach of the IC Act;
- contracts of insurance that are entered into or proposed to be entered into for the purposes of workers' compensation law continue to be exempt under the IC Act, notwithstanding that they also include cover against employer liability at common law to pay damages for employment-related personal injury; and
- contracts of insurance that include elements of cover that are exempted from the IC Act as well as cover that falls under the IC Act, are treated as exempt from the Act only in respect of the exempt elements.

Date of effect: On Royal Assent.

Schedule 2 — Electronic communication

1.5 It is proposed that the regulations under the *Electronic Transactions Act 1999* will be amended so that the IC Act will no longer be exempt from that Act. Schedule 2 to the Bill amends the IC Act to make technical changes to provisions in the IC Act regarding the giving of notices, documents and information, including a note that the *Electronic Transactions Act* will apply to permit electronic communication of notices or documents required to be given in writing.

Date of effect: Schedule 2 will take effect on a day to be fixed by Proclamation. This will permit coordination of the commencement with the proposed amendment to the *Electronic Transactions Regulations*.

Schedule 3 — Powers of ASIC

1.6 Schedule 3 to the Bill amends the IC Act to give the Australian Securities and Investments Commission (ASIC) a statutory right to intervene in any proceeding relating to matters arising under the IC Act and under Part 3 of the *Medical Indemnity (Prudential Supervision and Product Standards) Act 2003*.

Date of effect: On Royal Assent.

Schedule 4 — Disclosure and misrepresentations [The Date of effect of Schedule 4 has been refined in the Insurance Contracts Amendment Bill 2012 (No.)]

1.7 Schedule 4 to the Bill amends the IC Act so that:

- the mixed objective/subjective test in section 21 of the IC Act, which is used to determine if an insured has met their duty of disclosure, is clarified;
- the requirement to ask proposed insureds specific questions under section 21A as a condition of enforcing the insured's duty of disclosure will apply on renewal of an eligible contract of insurance (proposed new section 21B) as well as at inception (but not for a variation, a reinstatement or an extension), and 'catch all' questions will no longer be permitted;
- on renewal, insurers may choose to seek updates to answers previously provided by insureds, rather than asking specific questions again;
- an insurer must notify the insured, before the contract of insurance is entered into, that the duty of disclosure obligations continue until the time the policy is actually entered into;
- the IC Act provides that a form of words may be prescribed by regulation for use by insurers to inform persons of their duty of disclosure obligations; and
- any person who is not the insured but proposes to become a life insured under a contract of life insurance is subject to a duty to disclose, as well as a duty not to misrepresent, and the insurer must give this person notice of the duty before the contract is entered into;
- a failure to disclose by the proposed life insured will be imputed to the insured.

Date of effect: ~~The amendments take effect 18 months after the date of Royal Assent. This delay in commencement is to allow insurers an opportunity to amend their business practices in response to the new rules regarding the operation of the duty of disclosure and notification of that duty.~~

Schedule 5 — Remedies of insurers: life insurance contracts

1.8 The IC Act contains provisions that prescribe remedies for insurers that may be used where a person who became insured under a contract of insurance either misrepresented or did not disclose matters that should have been disclosed prior to entering into the contract. Section 28 deals with general insurance and section 29 deals with life insurance.

1.9 In some cases, the remedies in respect of bundled contracts of life insurance are inappropriate. Schedule 5 to the Bill amends the IC Act so that:

- the remedies in section 29 are limited to contracts of life insurance that contain, or will contain, a surrender value or provide cover in respect of the death of a life insured — other types of life insurance are dealt with under a new subsection 28(1A) that offers similar remedies to section 28 in its current form;
- life insurance contracts that combine more than one type of cover and more than one life insured are ‘unbundled’ for the purpose of applying the relevant remedies for non-disclosure or misrepresentation;
- the insurer can avoid a life insurance contract to which section 29 applies on the basis of non-disclosure or misrepresentation only if the insured would not have entered that particular contract (as opposed to the current standard of *any* life insurance contract) on any terms;
- insurers are entitled to change the expiration date of a life insurance contract (all types of life insurance, whether governed by new subsection 28(1A) or by section 29) where that date has been calculated by reference to the insured’s incorrectly-stated date of birth; and
- the statutory framework in the IC Act for cancellation of general insurance contracts will be extended to life insurance contracts (subject to forfeiture rights for non-payment of premiums under the *Life Insurance Act 1995*).

Date of effect: The amendments regarding unbundling of life insurance contracts and entitlement of insurers to change expiration dates and to cancel contracts of life insurance take effect on Royal Assent. The amendments regarding changes to the remedies for particular contracts of life insurance commence 12 months after the date of Royal Assent. The

delay in commencement is to allow insurers an opportunity to factor into their affairs the changes to available remedies.

Schedule 6 — Third parties

1.10 Schedule 6 to the Bill amends the IC Act so that:

- individuals who have rights under a contract of insurance ('third party beneficiaries') but who are not the insured, have access to particular rights and obligations currently held by insureds;
- third parties with damages claims against an insured or third party beneficiary who has died or cannot be found may recover directly against the insurer;
- ASIC will have powers to bring representative actions on behalf of third party beneficiaries;
- remedies for misrepresentation and non-disclosure are available in relation to contracts of life insurance that are offered as part of a group scheme that is unrelated to superannuation; and
- remedies are available in respect of any misrepresentation or non-disclosure that occurs between when an insured became a member of a superannuation or other group scheme and when the life insurance cover takes effect.

Date of effect: ASIC's powers to bring representative actions commence on the date of Royal Assent. The remainder of Schedule 6 commences 12 months after the date of Royal Assent. The delay in commencement is to allow insurers a reasonable opportunity to factor the new rights and obligations of third party beneficiaries into their business operations.

Schedule 8 — Subrogation

1.11 Schedule 7 to the Bill amends the IC Act so that:

- section 67 of the IC Act, which deals with the allocation of moneys recovered when an insurer exercises a right of subrogation in relation to an insurance claim, is revised to reflect wording of a draft provision dealing with subrogation proposed by the Australian Law Reform Commission in its Review of the *Marine Insurance Act 1909* (Cth); and

- Part VIII of the IC Act, which relates to subrogation, applies to claims made by third party beneficiaries as well as by insureds.

Date of effect: Schedule 7 commences six months after the date of Royal Assent. The delay in commencement is to allow insurers an opportunity to factor the new rules regarding subrogation into their business operations.

Financial impact statement

1.12 The Insurance Contracts Amendment Bill 2010 will have no financial impact on the Commonwealth.

Chapter 1

Notes on clauses

Schedule 1 — Scope and application

2.1 Schedule 1 to the Bill contains a range of provisions to change and/or clarify the scope and application of the IC Act. The provisions relate to:

- breaches of implied terms and the duty of utmost good faith (including extending the duty to third party beneficiaries);
- including a definition of ‘third party beneficiary’;
- exemptions for ‘bundled’ workers’ compensation contracts; and
- application of exemptions to ‘bundled’ contracts generally.

Part 1 — Duty of utmost good faith

Breach of the duty of utmost good faith

2.2 There is implied into all contracts of insurance, pursuant to section 13 of the IC Act, a provision that requires each party to that contract of insurance to act with the utmost good faith towards the other party in respect of any matters arising under or in relation to the contract.

2.3 Under the current law, parties to a contract of insurance may enforce compliance with this implied duty of utmost good faith through private legal action. However, this may present too great an expense for some parties and does not provide long-term solutions to systemic breaches of utmost good faith committed over time.

2.4 Item 4 in Part 1 of Schedule 1 inserts a subsection (2) in section 13 of the IC Act to address this issue by making a breach of the duty of utmost good faith a breach of the IC Act. The amendment allows ASIC to commence or continue representative action on behalf of an insured against an insurer, pursuant to section 55A of the IC Act. Pre-conditions to ASIC undertaking representative action on behalf of an insured are that the insured or insureds have suffered damage or there has been a breach of the IC Act.

2.5 The amendments to section 13 will also have the result that breaches of the duty of utmost good faith (and consequently of the IC Act) by an insurer may enable ASIC to access various remedies under the *Corporations Act 2001* in relation to Australian Financial Services Licence holders. These remedies include a banning order under section 920A of the Corporations Act, suspension or cancellation of the insurer's financial services licence, the imposition of conditions on the licence or the acceptance of an enforceable undertaking not to act in a particular manner. Item 5 will insert new section 14A in the IC Act, to avoid any doubt that the remedies are available for breaches of the duty of utmost good faith by an insurer in the handling or settlement of a potential claim. Arguably, regulations made under the Corporations Act in relation to the treatment of claims handling and settlement for the purposes of Chapter 7 of the Corporations Act may imply otherwise.

2.6 Banning orders made by ASIC have the effect of prohibiting the affected person from providing all financial services, or one or more specified types of financial service. They may be permanent or last only for a specified period. An example of the type of conduct leading to a permanent banning order is a pattern of persistent contraventions that indicate systemic failures or a general lack of understanding of, and regard for, compliance. Isolated breaches of the duty would not be expected to result in ASIC pursuing a banning order.

2.7 A breach of the IC Act for failure to comply with the duty of utmost good faith implied into all contracts of insurance is not an offence against the IC Act, nor does it attract any penalty under the IC Act.

Third party beneficiaries

2.8 Third party beneficiaries are not the insured under a contract of insurance but may be specified or referred to in its terms, either individually or as part of a class, as persons to whom any benefits provided by the contract extend. It follows therefore that they should have access to some of the rights and obligations under the IC Act that extend to insureds.

2.9 As third party beneficiaries are not parties to the contract of insurance, they do not benefit from the duty of utmost good faith, which is implied by the current section 13.

2.10 New subsections 13(3) and 13(4) (see item 4 in Part 1 of Schedule 1) address this by extending the duty of utmost good faith to third party beneficiaries; however, the duty only commences after the contract is entered into. This is because applying the duty pre-contractually would be impractical. Further, the duty of utmost good faith will be of most relevance for third party beneficiaries where they

wish to make a claim under a contract of insurance, as countenanced by subsection 48(2).

2.11 Item 2 of Part 1 of Schedule 1 inserts a definition of ‘third party beneficiary’ in subsection 11(1) of the IC Act.

Application

2.12 By operation of item 6 in Part 1 of Schedule 1, the amendments in Part 1 apply as follows:

to a contract of insurance that was originally entered into after the commencement of item 6;

to a contract of general insurance that was originally entered into before the commencement of item 6 and is renewed after that commencement; and

if the contract is a contract of life insurance that was originally entered into before the commencement of this item and is varied after that commencement to increase a sum insured under the contract, or to increase the number of life insureds under the contract, or to provide one or more additional kinds of cover; then the contract is treated, to the extent of the variation, as if it had been originally entered into after the commencement of item 6, and the amendments apply to the contract to the extent of the variation.

2.13 By operation of clause 2 of the Bill, item 6 in Part 1 of Schedule 1 commences on the day the Act receives the Royal Assent.

Part 2 — ‘Bundled’ workers’ compensation contracts

2.14 Paragraph 9(1)(e) of the IC Act exempts from the scope of the Act actual or proposed contracts of insurance that have been entered for the purposes of a state or territory law that relates to workers’ compensation or compensation for death or injury to a person arising from the use of a motor vehicle.

2.15 In practice, some contracts of insurance offer employees cover of the type described in paragraph 9(1)(e) and another type of cover. A particular example is contracts of insurance that bundle both cover for compulsory workers’ compensation purposes and cover for liability to employees at common law arising from employment-related personal injury.

2.16 The question arises as to whether such ‘bundled’ contracts of insurance are exempt or not from the scope of the IC Act. The Review

Panel recommended that, in the case of the example described above, the most effective solution to overcome uncertainty about application is to make the entire contract exempt from the scope of the IC Act. In other examples of contracts of insurance that bundle exempt and non-exempt types of cover, the Review Panel considered it not desirable to rule the entire contract either in or out of the scope of the Act. That situation is dealt with in Part 3 of Schedule 1.

2.17 Item 7 in Part 2 of Schedule 1 includes a new paragraph 9(1)(f) that exempts from the operation of the IC Act insurance contracts entered into (or proposed to be entered into) that bundle compulsory workers' compensation cover together with cover for an employer's liability at common law for damage suffered due to employment-related personal injury.

2.18 By operation of item 8 in Part 2 of Schedule 1, the amendments in Part 2 apply as follows:

(a) to a contract of insurance that was originally entered into after the commencement of item 8; and

to a contract of general insurance that was originally entered into before the commencement of item 8 and is renewed after that commencement.

2.19 By operation of clause 2, item 8 in Part 2 of Schedule 1 commences on the day the Act receives the Royal Assent.

Part 3 — 'Bundled' contracts generally

2.20 A contract of insurance may contain one or more types of cover to which the IC Act would *not* apply if they were contained in individual contracts, together with one or more types of cover to which the IC Act would apply if they were contained in individual contracts.

2.21 As was the case for the bundled contracts of insurance dealt with specifically in Part 2 of Schedule 1 described above, the Review Panel recommended that the exemption from the scope of the IC Act in subsection 9(1) of the Act be applied to each type of cover in a bundled insurance policy as if it were a separate contract.

2.22 Item 9 in Part 3 of Schedule 1 inserts new subsections 9(1A), 9(1B) and 9(1C). Under the new subsections, contracts of insurance that contain more than one type of cover, one of which is exempted and one of which is not (for this discussion called Cover A and Cover B respectively), would contain some terms that relate solely to Cover A,

some that relate solely to Cover B and some that relate to both Cover A and Cover B.

2.23 To create ‘unbundled’ contracts for the purposes of applying the exemption provisions, two notional contracts would be constructed. The first notional contract would comprise only those terms of the initial contract that are relevant to Cover A. The notional contract would also contain, as a consequence of subsection 9(1C), any terms of the initial contract that are relevant to both Cover A and Cover B.

2.24 Similarly, the second notional contract would comprise those terms of the initial contract that are relevant to Cover B only and the terms that are relevant to both Cover A and Cover B.

2.25 When the contents of the notional contracts are determined, the exemption provisions in subsection 9(1) are applied to each as if that contract were a separate contract of insurance or proposed contract of insurance.

2.26 It may be that there are more than two types of cover bundled within a contract of insurance, in which case more than two notional contracts of insurance will need to be developed at the first stage. However, irrespective of whether there are two or more kinds of exempt covers, or two or more kinds of non-exempt covers, or both, the result of applying the unbundling process in subsections 9(1A) and 9(1C) is that only those contractual terms that relate to the exempt cover type(s) are exempt from the operation of the IC Act.

2.27 New subsection 9(1B) applies a different rule for unbundling if one of the types of cover is a cover that is referred to in new paragraph 9(1)(f) (described in paragraph 3.17 above). This different treatment is necessary to ensure that directors’ liability cover (subparagraph 9(1)(f)(ii)) would only be exempted from the scope of the IC Act where it was bundled with compulsory workers’ compensation cover (subparagraph 9(1)(f)(i)).

2.28 By operation of item 10 in Part 3 of Schedule 1, the amendments made by Part 3 apply as follows:

- (a) to a contract of insurance that was originally entered into after the commencement of item 8 (the day the Act receives the Royal Assent);
- (b) to a contract of general insurance that was originally entered into before the commencement of item 10 and is renewed after that commencement; and

- (c) if the contract is a contract of life insurance that was originally entered into before the commencement of item 10 and is varied after that commencement to increase a sum insured under the contract, or to increase the number of life insureds under the contract, or to provide one or more additional kinds of cover; then the contract is treated, to the extent of the variation, as if it had been originally entered into after the commencement of this item, and the amendments apply to the contract to the extent of the variation.

2.29 By operation of clause 2, item 10 in Part 3 of Schedule 1 commences on the day the Act receives the Royal Assent.

Schedule 2 — Electronic communication

2.30 The Review Panel analysed the increasing use of electronic communications in the context of the IC Act. Currently, the IC Act is exempt from the coverage of most of the operative parts of the *Electronic Transactions Act 1999* (the ET Act), which provides that, in general, where a Commonwealth law requires a notice to be given in writing, then it may be given by electronic communication if certain conditions are met.

2.31 For example, subsection 9(1) of the ET Act provides that any communication required by a Commonwealth Act may only be done electronically if:

- at the time the information was given, it was reasonable to expect that the information would be readily accessible so as to be useable for subsequent reference; and
- the person to whom the information is required to be given consents to the information being given by way of electronic communication.

2.32 Section 14 of the ET Act contains rules about time and place of receipt and dispatch of electronic communications.

2.33 The Review Panel expressed support for the notion of updating the IC Act to allow for communication by electronic means. A proposed amendment to the *Electronic Transactions Regulations 2000* is expected to remove the current exemption, so that communications under the IC Act are subject to the ET Act. Schedule 2 to the Bill amends various provisions of the IC Act to recognise that the IC Act will be subject to the ET Act.

2.34 For the sake of consistency of terms in sections 70, 71 and 72 of the IC Act dealing with notices, items 2 to 6 of Schedule 2 remove references to ‘statement’ (wherever occurring). The concept of a ‘statement’ is covered by the term ‘notice or other document’.

2.35 Item 7 of Schedule 2 repeals the current section 72 of the IC Act (which is concerned with legibility of writing) and substitutes an expanded section 72. The purpose of this expansion is so that the regulation-making power in section 72 may deal not only with the content and legibility of the notice or other document itself, but also with material that may accompany the notice or other document or information. The power is intended to permit the making of regulations to ensure that the content of statutory notices under the IC Act is able to be digested by the recipient without interruption or distraction by other material provided with the notice.

2.36 Current section 77 of the IC Act applies generally in relation to notices or other documents or information that are required or permitted to be given by the IC Act. The section sets out the methods that may be used depending on whether the person to whom the notice or other document is to be given is a body corporate or a natural person. Subsection 77(2) also includes a rule regarding the time of receipt of a notice of cancellation of a contract of insurance.

2.37 Item 8 of Schedule 2 repeals current section 77 of the IC Act and Item 1 is a consequential amendment to subsection 62(1). Item 7 largely replicates the content of section 77 as new section 72A, but removes the rule regarding notice by post of cancellation. Section 29 of the *Acts Interpretation Act 1909* deals with that subject. Section 72A is not intended to affect the operation of subsection 71(1), which covers situations where insurance is arranged by brokers acting for the insureds.

Application

2.38 By operation of item 9 of Schedule 2, the amendments in Schedule 2 apply to a notice or other document or information given to a person under the IC Act after the commencement of item 9 of Schedule 2.

2.39 By operation of clause 2, item 9 of Schedule 2 commences on the day the Act receives the Royal Assent.

Schedule 3 — Powers of ASIC

2.40 Part IA of the IC Act gives the Australian Securities and Investments Commission (ASIC) responsibility for the general administration of the IC Act and vests in ASIC a number of specific powers to support this role, such as the power to obtain documents.

2.41 Item 1 of Schedule 3 inserts a new section 11F into the IC Act that gives ASIC powers to intervene in matters arising under the Act. The provision is similar in form to the existing power that ASIC has to intervene in proceedings begun by other persons about matters arising under the *Corporations Act 2001* (section 1330). It allows ASIC to be represented in the proceedings by a staff member, a delegate, a solicitor or counsel.

2.42 By new section 11F, ASIC may also intervene in a matter arising under Part 3 of the *Medical Indemnity (Prudential Supervision and Product Standards) Act 2003*. Part 3 of the *Medical Indemnity (Prudential Supervision and Product Standards) Act 2003* enables ASIC (and also other parties) to make application to the court to enforce product standards for medical indemnity insurance. The expanded power would enable ASIC to intervene in any proceeding relating to matters arising under Part 3.

Application

2.43 By operation of item 2 of Schedule 3, the amendment made by Schedule 3 applies to a proceeding that is commenced after the commencement of item 2.

2.44 By operation of clause 2, item 2 of Schedule 3 commences on the day the Act receives the Royal Assent.

Schedule 4 — Disclosure and misrepresentations

2.45 Schedule 4 amends the manner in which the IC Act deals with particular types of disclosure and misrepresentations. The changes:

- clarify how the duty of disclosure test is applied;
- in relation to eligible contracts of insurance, amend the law to make the duty of disclosure apply on renewal of a contract of insurance and remove the option for insurers to ask ‘catch all’ questions’;
- amend the law regarding circumstances in which an insurer must provide an insured with a reminder as to when their duty of disclosure obligation applies; and
- in relation to contracts of life insurance, amend the law so insurers must give a potential life insured, who is not the insured under the relevant contract of insurance, notice of their duty of disclosure.

2.46 The changes made by Schedule 4 will require insurers to adjust various their business practices. This will take time to implement. Accordingly, the commencement of Schedule 4 is delayed by 18 months from Royal Assent in order to allow insurers time to implement the necessary changes to their systems and documents as required.

Part 1 — Insured’s duty of disclosure [This measure has been refined in the Insurance Contracts Amendment Bill 2012 (No.)]

2.47 Sections 21 and 21A of the IC Act are key provisions that govern the insured’s duty of disclosure obligations. Section 21 imposes a requirement on an insured, before a contract is entered into, to disclose various matters. What must be disclosed is determined by reference to a test that contains both subjective elements (what the insured knows to be relevant to the insurer’s decision) and objective elements (what a reasonable person in the circumstances could be expected to know would be relevant to the insurer’s decision).

~~2.48 — The mixed subjective/objective test has not been applied consistently. To help clarify its interpretation, item 1 in Part 1 of Schedule 4 expands the objective element of the test in paragraph 21(1)(b) of the IC Act to include a non-exclusive factor to which the court may have regard when determining whether a reasonable person in the circumstances could be expected to know a matter was relevant to the decision of the insurer whether to enter the contract of insurance. The~~

~~factor is the nature and extent of the insurance cover to be provided under the relevant contract of insurance.~~

Application

2.49 By operation of item 2 in Part 1 of Schedule 4, the amendment in Part 1 of Schedule 4 applies as follows:

- (a) to a contract of insurance that was originally entered into after the commencement of item 2;
- (b) to a contract of general insurance that was originally entered into before the commencement of item 2 and is renewed after that commencement; and
- (c) if a contract is a contract of life insurance that was originally entered into before the commencement of item 2 and is varied after that commencement to increase a sum insured under the contract, or to increase the number of life insureds under the contract, or to provide one or more additional kinds of cover; then the contract is treated, to the extent of the variation, as if it had been originally entered into after the commencement of this item, and the amendment applies to the contract to the extent of the variation.

2.50 By operation of clause 2, item 2 in Part 1 of Schedule 4 commences on the day after the end of the period of 18 months beginning on the day the Act receives the Royal Assent.

Part 2 — Eligible contracts of insurance

2.51 Section 21A of the IC Act supplements the general provisions regarding the duty of disclosure in section 21, but only in relation to certain ‘eligible contracts of insurance’. ‘Eligible contracts of insurance’ are prescribed by regulations made under the IC Act. They include contracts that provide cover commonly sought by individual consumers, such as motor vehicle, home contents and travel insurance.

2.52 For an insurer to be able to rely on compliance by an insured with their duty of disclosure, section 21A requires the insurer to ask the insured specific questions that are relevant to the insurer’s decision whether to accept the risk and, if so, on what terms. However, it is also currently permissible for the insurer to ask the insured a ‘catch all’ question, which requires an insured to disclose ‘exceptional circumstances’ that a reasonable person could be expected to know would be relevant to the insurer’s decision whether to accept the risk, and about which would be unreasonable for the insurer to ask a specific question (subparagraph 21A(4)(b)(iii)). The current ability to ask ‘catch all’

questions tends to undermine the benefits for insureds of the framework for eligible contracts of insurance. Insurers should be in a position to decide what matters are material to their decision to provide eligible contracts of insurance and formulate specific questions accordingly. In the event that an insurer is unable to foresee a matter that is relevant to their decision whether to accept the risk of a particular contract, then it is difficult to justify expecting an unsophisticated insured to realise its relevance.

2.53 Section 21A only applies when a contract is first entered into — it currently has no application to renewals (subsection 21A(1)). However, for the purposes of other provisions, a renewal is treated as entry into a new contract (subsection 11(9)). Accordingly, renewal of an eligible contract of insurance would trigger the general duty of disclosure provisions under section 21. This can be onerous for insureds in comparison with, for example, the framework for eligible contracts under section 21A.

2.54 The provisions in Part 2 of Schedule 4 are designed to:

- remove the ability of insurers to ask ‘catch all’ questions in relation to eligible contracts; and
- apply enhanced rules for the duty of disclosure on original inception and renewal of eligible contracts.

2.55 Item 4 in Part 2 of Schedule 4 substitutes a new section 21A and inserts a new section 21B.

2.56 In relation to the original entering into of an eligible contract of insurance, new section 21A provides that the insurer is required to ask the insured to answer one or more specific questions that are relevant to the insurer’s decision whether or not to accept the risk, and is taken to have waived compliance with the insured’s duty of disclosure if it does not do so. Further, asking ‘catch all’ questions covering any other matter outside the specific requests will result in a waiver of the duty of disclosure with respect to the other matters. The operation of new section 21A is not triggered by a variation, reinstatement or extension of a contract of insurance.

2.57 New section 21B applies in relation to the renewal of an eligible contract of insurance (new subsection 21B(1)). New subsections 21B(2) to (5) deal with the position of the insurer — in particular in what circumstances they are taken to have waived compliance with the duty of disclosure. In relation to the renewal of an eligible contract of insurance, new section 21B(2) requires an insurer wishing to rely on the insured’s duty of disclosure to:

- ask specific questions, just as they may on the original entering into of a contract; and/or
- provide the insured, prior to renewing the contract, with a copy of any matters previously disclosed by the insured in relation to the contract, and request the insured to disclose any changes to those matters or to indicate if there are no such changes.

If the insurer does neither of those things, new subsection 21B(3) provides that they are taken to have waived compliance with the duty of disclosure in relation to the renewed contract (subject to new subsection 21B(11), which deals with the effects of non-disclosures and misrepresentations that occurred on previous renewals or original inception).

2.58 New subsections 21B(4) and 21B(5) deal with ‘catch all’ questions. Asking ‘catch all’ questions covering other matters addition to asking specific questions and/or seeking updates to information previously disclosed will result in waiver of compliance with the duty of disclosure with respect to the other matters.

2.59 New subsections 21B(6) to (8) deal with the position of the insured — in particular, in what circumstances they are taken to have complied with the duty of disclosure.

2.60 Subsection 21B(6) deals with an insured who is only asked specific questions. In that case, to be taken to have complied with the duty of disclosure in relation to the renewed contract if they disclose, in response to each specific question, matters that are known to them and matters that a reasonable person in the circumstances would be expected to have disclosed in answer to the question.

2.61 Subsection 21B(7) deals with an insured who is only asked to update matters previously disclosed. In that case, to be taken to have complied with the duty of disclosure in relation to the renewed contract the insured must disclose any change to the matter or inform the insurer if there is no change.

2.62 Subsection 21B(8) deals with an insured who is both asked specific questions and asked to update answers previously provided. In that case, the insured must both disclose responses to the specific questions (similar to the requirements of subsection 21B(6)) and advise the insurer of any change/no change to the matters (similar to the requirements of subsection 21B(7)).

2.63 Subsections 21B(6) to 21B(8) are all subject to new subsection 21B(11), which provides that compliance by an insured with

the duty of disclosure on a renewal does not mean that a failure to comply with the duty of disclosure on original inception or a previous renewal is negated. For example, suppose when originally applying for a home buildings policy, an insured breaches the duty of disclosure in relation to providing information on the main construction materials used in the home. At a subsequent renewal, the insurer seeks updates to various matters but does not ask the insured to update the information previously provided on main construction materials, because they are unlikely to change between inception and renewal. In such a case, even though the insured may be taken to comply with the duty of disclosure in respect of the renewed contract by providing all updates as requested, the effect of subsection 21B(11) is that compliance with the duty under the renewed contract does not operate to negate the earlier failure. The intention of this provision is to permit insurers to continue to rely on the accuracy, *as at the time of inception or the previous renewal*, of matters disclosed on inception and previous renewals. Otherwise, insurers seeking to rely on any information previously provided by an insured (such as, for example, what a home is constructed of) would need to seek updates to every such matter at every renewal, which would be onerous and time consuming for both insurers and insureds. For the sake of clarity, the rule in subsection 21B(11) should not be taken to imply that an insured who has complied with the duty of disclosure previously is under a continuing obligation to update matters that have changed at renewal, unless specifically requested to do so. If an insurer wishes to ensure that information is updated at renewal, they will need to either ask the insured a specific question regarding the matter, or ask the insured to update the information previously provided.

2.64 Some insureds may not respond to request to update matters previously provided, but nevertheless pay the renewal premium. If an insurer seeks an update to a matters previously provided but the insured provides no response before the contract is renewed, then new subsection 21B(9) operates so that the insured is taken to have advised the insurer that there is no change to the matter. New subsection 21B(10) disappplies the provisions of subsections 21(3) and 27, which would otherwise provide for some consequences of an insured's failure to answer questions. Subsection 21B(10) also applies if the insured advises the insurer that there is no change to a matter.

Application

2.65 By operation of subitem 4(1) in Part 2 of Schedule 4, the amendments in Schedule 4 relating to the insertion of proposed new section 21A apply to an eligible contract of insurance originally entered into after the commencement of item 3.

2.66 By operation of subitem 4(2), the amendments in Schedule 4 relating to the insertion of proposed new section 21B apply to an eligible contract of insurance that is renewed after the commencement of item 3, regardless of when the contract was originally entered into.

2.67 By operation of clause 2, item 3 in Part 2 of Schedule 4 commences on the day after the end of the period of 18 months beginning on the day the Act receives the Royal Assent.

Saving of regulations

2.68 Item 5 in Part 2 of Schedule 4 provides for the saving of existing regulations made for the purpose of the definition of ‘eligible contract of insurance’ in current subsection 21A(9), as if they had been made for the purposes of the definition of ‘eligible contract of insurance’ (as inserted in subsection 21A(6)). By operation of item 3 in Part 2 of Schedule 4, the definition of ‘eligible contract of insurance’ is inserted in subsection 21A(6) of the IC Act.

Part 3 — Insurers’ duty to inform of duty of disclosure

Notification that the duty exists until contract begins

2.69 The insured has a duty of disclosure until the time at which the relevant contract of insurance is entered into. In normal circumstances this presents no difficulty because the insured provides information to the insurer a short time before the contract begins. This is not always the case.

2.70 In some instances, particularly where long term contracts of life insurance are involved, there may be a significant time lag (sometimes months) between the time a prospective insured submits information to an insurer — usually when making an application — and the time the policy is actually issued. During this period, circumstances may change, or events may occur, that need to be disclosed to the insurer in order for the insured to comply with the duty of disclosure.

2.71 If the insured fails to disclose those circumstances or events before the contract is entered into, then any claim they later make could be at risk due to their failure to comply with the duty of disclosure. The Review Panel recommended, in order to minimise the possibility of harsh outcomes, that prospective insureds should be reminded that the duty of disclosure extends until the time the relevant policy is entered into.

2.72 Current subsection 22(1) of the IC Act requires insurers to notify insureds about the duty of disclosure any time ‘before the contract is entered into’. Item 8 in Part 3 of Schedule 4 substitutes a new section 22,

providing that the insurer must clearly inform the insured of the general nature and effect of the duty of disclosure, and where relevant, the general nature and effect of sections 21A or 21B.

2.73 New subsection 22(2) requires insurers to inform proposed life insureds that they have a duty of disclosure. This includes information on the effect of proposed new section 31A (see below). Item 6 in Part 3 of Schedule 4 provides that the definition of a 'life insured' includes a proposed life insured.

2.74 New subsection 22(1) also makes it clear that any notification given to the insured pursuant to the section should explain that the duty of disclosure obligation applies until the time that the proposed contract is entered into (Item 8 in Part 3 of Schedule 4).

2.75 Item 8 also provides in new subsection 22(3) that where the insurer's acceptance, or counter-offer, in relation to the proposed contract of insurance, is made more than two months after the insured's most recent disclosure for the purposes of complying with their duty of disclosure, then along with the acceptance or counter-offer, the insurer must also provide the insured with a reminder that the duty of disclosure applies until the proposed contract (or, in the case of a counter-offer, the other contract) is entered into.

2.76 The addition of this reminder requirement in cases where there is a significant delay between the initial disclosure and the contract commencing is intended to promote disclosures being made current as at the contract date, so that the insurer is fully informed, and there can be an early renegotiation of the contract if necessary.

2.77 The additional reminder requirement imposed by new subsection 22(3) is not extended to a life insured, unless the life insured is also the contracting insured.

2.78 Item 8 in Part 3 of Schedule 4 provides under new subsection 22(4) that the form of writing used to inform a person of the matters referred to in subsection 22(1), and also for the reminder notice referred to in subsection 22(3), may be in accordance with the prescribed form, where the regulations prescribe a form of writing to be used for the purposes of section 22.

2.79 New subsection 22(5) applies such that an insurer that fails to comply with subsection 22(1) and, if applicable, subsection 22(2) will be precluded from exercising a right in respect of a failure by the insured to comply with their duty of disclosure under the contract, unless the particular failure is fraudulent. This is consistent with the current position in respect of insureds.

2.80 New subsection 22(6) and (7) deals with an insurer that fails to comply with subsection 22(3), which is the provision requiring a reminder notice in cases of delay between initial disclosure and the contract commencing. In those circumstances, the insurer is precluded from exercising a right in respect of a failure to disclose any ‘new matter’, defined as a matter that the insured first become aware of after their most recent disclosure (and which, therefore, may not have been disclosed as a result of the failure to provide the reminder notice).

2.81 Item 7 in Part 3 of Schedule 4 amends paragraph 11(10)(b) of the IC Act with the effect that section 22 (in the case of both general and life insurance) and section 40 (in the case of general insurance) does not require an insurer to give information to the insured at or before a variation of the relevant contract of insurance, except where the variation is involved in a renewal, extension or reinstatement of the contract, or if the varied contract will provide a kind of insurance cover that was not provided by the contract immediately before the variation. Section 22 will also continue to apply in the case of variation of a contract of life insurance if the variation will increase a sum insured in respect of the insured.

2.82 Subsection 11(10) operates notwithstanding subsection 11(9) of the IC Act, which provides that a reference in the Act to the ‘entering into’ of a contract of insurance includes a reference to, in the case of life insurance, the making of an agreement by the parties to extend or vary the contract, and in the case of any other contract of insurance, the making of an agreement by the parties to the contract to renew, extend or vary the contract, or to the reinstatement of any previous contract.

2.83 Under paragraph 11(10)(a) or (b) (as amended), the insurer may be taken to have satisfied the requirements of section 22 in relation to a renewal, extension or reinstatement if the insurer has previously given the information required by that section to the insured and certain other conditions are met. After the commencement of new section 22, the references in paragraphs 11(10)(a) and (b) to the information required under section 22 are to the information required under the new section 22. This means that, in most cases, the insurer will be required to comply with new section 22 in the case of a renewal, extension or reinstatement of a contract that was originally entered into before the commencement of new section 22, and also with respect to a variation of the kind referred to in amended paragraph 11(10)(b) (that is, new subparagraph 11(10)(b)(ii)).

Application

2.84 Item 9 in Part 3 of Schedule 4 provides that the amendments in Part 3 apply to a contract of insurance whether entered into after commencement of item 9, and to a contract of insurance that was

originally entered into before commencement of item 9 that is renewed, extended, varied or reinstated after that commencement.

2.85 By operation of clause 2, item 9 in Part 3 of Schedule 4 commences on the day after the end of the period of 18 months beginning on the day the Act receives the Royal Assent.

Part 4 — Non-disclosure by life insured

2.86 Contracts of life insurance are often entered into by one person to cover the life of another. A life insured under a contract of insurance may include persons who are not the insured and, therefore, not subject to duty of disclosure obligations under current law. Although not a contracting party, the person whose life is proposed to be insured (known as the ‘life insured’) will usually provide the insurer with information about matters such as their state of health, in order to assist the insurer to make a decision about whether, and on what terms, to issue the policy.

2.87 Section 25 of the IC Act provides that if, during the negotiations on a life insurance contract, a prospective life insured makes a misrepresentation, the IC Act takes effect as if the misrepresentation has been made by the contracting insured. However, the existing wording of section 25 only extends to misrepresentations

2.88 Non-disclosure can be similar in result to misrepresentation, in terms of the potential detrimental impact on an insurer’s decision to enter into the contract. Accordingly, item 10 in Part 4 of Schedule 4 inserts a new section 31A in the IC Act, which is similar in its effect to section 25, except that it covers non-disclosures by lives rather than misrepresentations made by them. The life insured’s duty of disclosure under new section 31A is similar to that applying to insureds under section 21, except any non-disclosure by a life insured is imputed to the insured. Like existing the duty of disclosure under section 21 for insureds, there is an exception applied for non-disclosure of matters that diminish the risk, are common knowledge, that the insurer knows or ought to know in the ordinary course of its business, or for which compliance with the duty is waived by the insurer.

Application

2.89 By operation of item 11 in Part 4 of Schedule 4, the amendment made by Part 4 of Schedule 4 applies as follows:

- (a) to a contract of life insurance that was originally entered into after the commencement of item 11; and

if a contract of life insurance that was originally entered into before the commencement of item 11 is varied after that commencement to increase a sum insured under the contract, or to increase the number of life insureds under the contract, or to provide one or more additional kinds of cover; then the contract is treated, to the extent of the variation, as if it had been originally entered into after the commencement of item 11, and the amendment applies to the contract to the extent of the variation.

2.90 By operation of clause 2, item 11 in Part 4 of Schedule 4 commences on the day after the end of the period of 18 months beginning on the day the Act receives the Royal Assent.

Schedule 5 — Remedies of insurers: life insurance contracts

2.91 Schedule 5 amends the way in which the IC Act deals with remedies for life insurers in cases of misrepresentation or non-disclosure by insureds prior to entry into the contract of life insurance. The amendments, which are designed to make the remedies more flexible and tailored than those that are currently available, apply to:

- contracts of life insurance that provide two or more kinds of insurance cover, or a single kind of cover that is provided on different terms (for example, an element that is underwritten and another element that is not) or cover for two or more life insureds;
- allow the remedies to be applied to each different element of a bundled life insurance contract as if each element or aspect were a separate policy;
- introduce a distinction between the remedies applying to different forms of life insurance cover, so that the remedies applicable under section 29 would only apply to ‘traditional’ life insurance policies (that is, life insurance contracts with a surrender value or that provide cover in respect of death) and remedies similar to the remedies applying to general insurance contracts would apply to all other forms of life insurance, that is, contracts other than contracts with a surrender value or providing death cover; and
- expand the range of remedies that are available to a life insurer in cases where the misrepresentation involves a misstatement of the date of birth of a life insured under the contract.

Part 1 — ‘Unbundling’ of contracts [the approach taken in respect to the unbundling of life insurance contracts has been refined in the Insurance Contracts Amendment Bill 2012 (No.)]

2.92 Contracts of life insurance often ‘bundle’ different types of protection against more than one type of insurable event resulting from death, sickness or accident in the one contract. An application seeking cover for each type of insurable event will be ‘unbundled’ for separate consideration by an insurer in relation to each type of risk, and different factors will be taken into account as part of the underwriting process.

2.93 For example, an applicant may present with a family medical history of a condition that is well recognised as a risk factor in the development of a debilitating disease, but a disease that is unlikely to result in premature death. In those circumstances, the insurer is likely to accept a death cover component without a loading or exclusion, but the income protection cover would be offered with a modification to the policy terms or with a premium loading, in response to the additional risk caused by the family history of the condition.

2.94 Any misrepresentation or non-disclosure that affects one aspect of the insurance cover may not be relevant to the other. However, as currently drafted, the remedies that are available, such as for avoidance or variation of the contract, must be applied to the contract as a whole. This can be to the significant disadvantage of an insured and unnecessarily restrict the remedial options for an insurer.

~~2.95 — Item 1 in Part 1 of Schedule 5 inserts a new section 27A into the IC Act, which provides that if a contract of life insurance contains two or more kinds of insurance cover or two or more life insureds, the remedies in Division 3 of Part IV for misrepresentation and non-disclosure apply to each type of cover or each life insured, as if the contract contained only the one kind of cover or provided cover in relation to only one life insured. Therefore, if a contract contains cover in respect of death and cover in respect of total and permanent disability, the remedies for misrepresentation or non-disclosure would apply to each type of cover and each life insured, separately, as required.~~

~~2.96 — Similarly, new subsection 27A(3) provides that where a life insurance contract contains an element of cover that is underwritten on particular terms and another element that is either not underwritten or is underwritten on different terms, the elements are to be regarded as separate kinds of cover for the purposes of unbundling in section 27A. The intention of that provision is to permit unbundling under section 27A in circumstances such as where a person has cover under a group life scheme that is automatically provided to all members of the scheme and which is either not underwritten at all, or underwritten by, for example, a~~

~~short form questionnaire, in addition to additional ‘top up’ cover that is underwritten through, for example, a comprehensive questionnaire and full medical examination. This allows any remedies in respect of non-disclosure and misrepresentation in relation to obtaining the top up cover to be utilised by a life insurer in relation to the top up only, without affecting the person’s automatic cover.~~

Application

2.97 By operation of item 2 in Part 1 of Schedule 5, the amendments made by Part 1 of Schedule 5 apply to a contract of life insurance whether originally entered into before or after commencement of item 2.

2.98 By operation of clause 2, item 2 in Part 1 of Schedule 5 commences on the day the Act receives the Royal Assent.

Part 2 — Remedies for non-disclosure and misrepresentation [This measure has been refined in the Insurance Contracts Amendment Bill 2012 (No.)]

2.99 The current section 29 of the IC Act lists remedies that may be applied by life insurance providers in cases of misrepresentation and non-disclosure. Whilst suitable for ‘traditional’ kinds of life insurance policy (that is, those with a surrender value or providing death cover), the current provision is not well-suited to many types of life insurance that are now made available (for example, short-term cover for income protection or total and permanent disability). In many cases, misrepresentation or non-disclosure in respect of non-traditional types of life insurance policy would be better dealt with through remedies akin to those available for general insurance policies.

2.100 Surrender value refers to the cash amount payable by the life insurance company to the policy owner in the event a policy is voluntarily terminated before its maturity or the death of the insured person. They are common in traditional ‘whole of life’ and ‘endowment’ investment-style insurance policies. The *Life Insurance Act 1995* sets the minimum standard for the calculation of a surrender value.

2.101 — ~~Item 5 in Part 2 of Schedule 5 inserts a new subsection 29(1A), which will define contracts of life insurance, for the purposes of applying the remedies in section 29, as contracts of life insurance that either have a surrender value or provides insurance cover in respect of the death of a life insured.~~

2.102 — ~~Item 4 in Part 2 of Schedule 5 inserts new section 28(1A) into section 28 of the IC Act to provide the same remedies for life insurance contracts, which do not have a surrender value or provide death cover, as~~

are available with respect to general insurance policies under section 28. Notes to items 4 and 5 indicate that new headings are inserted for section 28 and in relation to subsection 28(1), new subsection 28(1A) and revised section 29.

2.103 — Item 8 in Part 2 of Schedule 5 amends the reference to ‘a contract’ in subsection 29(3) of the IC Act to ‘the contract’. This change is in response to a concern that, on one interpretation of the current subsection 29(3), the insurer can only avoid a contract for non-disclosure or misrepresentation if they show that they would not have been prepared to enter *any* contract of life insurance with the insured, had the insurer known the true facts. The intention of this change is to clarify that the insurer should be able to avoid the particular contract if they would not have extended cover of the risk proposed on any terms, had the true facts been known. The fact that the insurer may still have been willing to offer cover of a different type of risk had the true facts been known should not mean their right to avoid the particular contract for misrepresentation or non-disclosure under subsection 29(3) is lost. This issue is avoided by referring to ‘the contract’ rather than ‘a contract’.

2.104 — Items 6 and 7 make some minor technical drafting changes to the wording of section 29.

Application

2.105 By operation of item 9 in Part 2 of Schedule 5, the amendments made by Part 2 apply as follows:

- (a) to a contract of life insurance that was originally entered into after the commencement of item 9; and
- (b) if a contract of life insurance that was originally entered into before the commencement of item 9 is varied after that commencement to increase a sum insured under the contract, or to increase the number of life insureds under the contract, or to provide one or more additional kinds of cover, then the contract is treated, to the extent of the variation, as if it had been originally entered into after the commencement of item 9, and the amendments apply to the contract to the extent of the variation.

2.106 By operation of clause 2, item 9 in Part 2 of Schedule 5 commences on the day after the end of the period of 12 months beginning on the day the Act receives the Royal Assent.

Part 3 — Remedy for misstatement of date of birth

2.107 Section 30 of the IC Act contains specific remedies for life insurers in circumstances where the date of birth of one or more life insureds was incorrectly stated at the time the contract was entered into. It covers situations where age was understated or overstated, and allows the insurer, when the true date of birth is known, to adjust the sum insured or reduce the premium payable. Item 10 in Part 3 of Schedule 5 inserts a new subsection 30(3A) in the IC Act to establish an additional remedy for an insurer in circumstances addressed by section 30. Under this new option, an insurer may vary the contract by changing its expiration date to a date calculated on the basis of the correct date of birth. This means that neither the amount insured nor the premium payable needs to be modified.

2.108 Item 11 in Part 3 of Schedule 5 amends subsection 30(4), so that a variation of the contract as permitted under the new subsection 30(3A) is taken to have occurred from the time the contract was entered into. This is in accordance with the rule regarding the existing remedies in subsection 30(2).

Application

2.109 By operation of item 12 in Part 3 of Schedule 5, the amendments made by Part 3 apply as follows:

- (a) to a contract of life insurance that was originally entered into after the commencement of item 12; and
- (b) if a contract of life insurance that was originally entered into before the commencement of item 12 is varied after that commencement to increase a sum insured under the contract, or to increase the number of life insureds under the contract, or to provide one or more additional kinds of cover, then the contract is treated, to the extent of the variation, as if it had been originally entered into after the commencement of item 12, and the amendments apply to the contract to the extent of the variation.

2.110 By operation of clause 2, item 12 in Part 3 of Schedule 5 commences on the day the Act receives the Royal Assent.

Part 4 — Cancellation of contracts

2.111 Section 60 of the IC Act provides the circumstances in which an insurer may cancel a contract of general insurance. There is no section 60 equivalent for contracts of life insurance, and no provision in the IC Act that allows a life insurer to cancel a policy of life insurance for any reason. Cancellation of life insurance contracts for non-payment of

premiums ('forfeiture') is regulated by the *Life Insurance Act 1995*. Rights of cancellation for other reasons (for example, a fraudulent claim) are currently left to the common law.

2.112 In response to court decisions regarding rights of cancellation regarding life insurance contracts under the common law, the Bill will introduce a statutory framework for life insurance cancellation similar to that applying to general insurance. Item 13 in Part 4 of Schedule 5 inserts after section 59 in Part VII of the IC Act (Expiration, renewal and cancellation) a new section (section 59A — Cancellation of certain contracts of life insurance) providing for a life insurer to cancel a life insurance contract for the same reasons that an insurer may cancel a contract of general insurance, except in relation to non-payment of a premium. A note to new paragraph 59A(d) indicates that section 210 of the *Life Insurance Act 1995* deals with forfeiture of a contract of life insurance because of non-payment of a premium.

2.113 Current section 63 prohibits an insurer from cancelling a contract of general insurance and any purported cancellation in contravention of section 63 is void. Item 14 in Part 4 of Schedule 5 amends section 63 to provide for a mirror contravention in relation to a purported cancellation (contrary to section 63) of a contract of life insurance. Accordingly, a cancellation of a life insurance contract (other than under the *Life Insurance Act 1995*) will have to be effected in accordance with the requirements of section 59A. This change does not affect the notice requirements under existing section 59.

Application

2.114 By operation of item 15 in Part 4 of Schedule 5, the amendments made by Part 4 of Schedule 5 apply to a contract of life insurance that was originally entered into after the commencement of item 15.

2.115 The amendment to section 63 made by item 14 does not alter the law applying to general insurance, so that amendment applies to general insurance contracts entered into before or after the commencement of item 15.

2.116 By operation of clause 2, item 15 in Part 4 of Schedule 5 commences on the day the Act receives the Royal Assent.

Schedule 6 — Third parties

2.117 Third parties may be persons that are specified in a contract of insurance (whether by name or otherwise) as being persons to whom cover provided by the contract extends ('third party beneficiaries') or they

may be third parties against whose claims an insured or third party beneficiary has insurance cover. Schedule 6 contains a series of amendments designed to alter the rights and obligations of third parties under the IC Act.

Part 1 — Requests by third party beneficiaries to insurers for information

2.118 Under current section 41 of the IC Act, an insured that has made a claim under a contract of liability insurance may require the insurer to inform them in writing:

- whether the insurer admits that the contract applies to the claim; and
- if the insurer so admits, whether the insurer proposes to conduct, on behalf of the insured, the negotiations and any legal proceedings in respect of the claim made against the insured.

2.119 Item 1 in Part 1 of Schedule 6 substitutes a new section 41 in substantially the same terms as the current section 41, except that it is extended to give third party beneficiaries (as claimants) the same rights as insureds under the section.

Application

2.120 By operation of item 2 in Part 1 of Schedule 6, the amendment made by Part 1 of Schedule 6 applies to a contract of liability insurance that was originally entered into after commencement of item 2. The amendment also applies to a contract of liability insurance that was originally entered into before the commencement of item 2 and is renewed after that commencement.

2.121 By operation of clause 2, item 2 in Part 1 of Schedule 6 commences after the end of the period of 12 months beginning on the day the Act receives the Royal Assent.

Part 2 — Insurer's defences in actions by third party beneficiaries

2.122 Section 48 of the IC Act deals with, amongst other things, the defences available to a general insurer against a claim by a third party beneficiary. Section 48AA makes similar provision regarding contracts of life insurance offered in connection with Retirement Savings Accounts (RSAs).

2.123 Items 3 and 4 in Part 2 of Schedule 6 amend (including by repealing and substituting) subsections 48(1) and 48(2) so that they use the term ‘third party beneficiary’, now defined in section 11 (see item 1 in Part 1 of Schedule 1), but the substance of the subsections is unchanged. There are similar amendments to section 48AA in items 7 and 8 in Part 2 of Schedule 6.

2.124 Section 48AA is worded similarly to section 48, except that it deals with the defences a life insurer has against a claim by third party beneficiaries in relation to a contract of life insurance taken out by an RSA provider. To ensure greater consistency in the wording of sections 48AA and 48, items 5 and 9 amend paragraphs 48(2)(a) and 48AA(2)(a), so that the wording of the two sections mirror each other.

2.125 There has been some doubt as to whether subsection 48(3), and as a consequence subsection 48AA(3), allow for claims by third party beneficiaries to be tainted by the wrongful conduct of an insured. There is also doubt as to whether an insurer may raise pre-contractual conduct, such as a breach of the duty of disclosure, in assessing a claim by a third party beneficiary.

2.126 The intent of sections 48 and 48AA (as amended) is that third party beneficiaries should be in no better position, in terms of their ability to claim, than the insured. An insurer should be entitled to raise defences relating to the conduct of an insured, including conduct occurring prior to the time the contract was entered into.

2.127 To give effect to these intentions, items 6 and 11 in Part 2 of Schedule 6 amend subsections 48(3) and 48AA(3) respectively, to make it clear that, in defending an action by a third party beneficiary:

- an insurer may raise defences relating to the conduct of the insured; and
- the conduct that may be raised may have occurred either after the contract was entered into or before (for example, non-disclosure).

Application

2.128 By operation of subitem 12(1), the amendments made by items 3 to 6 in Part 2 of Schedule 6 apply to a contract of general insurance originally entered into after the commencement of subitem 12(1).

2.129 The amendments also apply to a contract of general insurance that was originally entered into before the commencement of subitem 12(1) and is renewed after that commencement.

2.130 By operation of subitem 12(2), the amendments made by items 7 to 11 in Part 2 of Schedule 6 apply to a contract of life insurance that was originally entered into after the commencement of subitem 12(2). If a contract of life insurance that was originally entered into before the commencement of subitem 12(2) is varied after that commencement to increase a sum insured under the contract, or to increase the number of life insureds under the contract, or to provide one or more additional kinds of cover, then the contract is treated, to the extent of the variation, as if it had been originally entered into after the commencement of subitem 12(2), and the amendments made by items 7 to 11 apply to the contract to the extent of the variation.

2.131 By operation of clause 2, item 12 in Part 2 of Schedule 6 commences at the end of the period of 12 months beginning on the day the Act receives the Royal Assent.

Part 3 — Rights and obligations of third party beneficiaries under life insurance contracts

2.132 Section 48A of the IC Act applies to contracts of life insurance that are effected on the life of one person but expressed to be for the benefit of another person (a third party beneficiary). As part of its review, the Review Panel recommended a series of amendments be made to section 48A in response to recent developments in the insurance industry.

2.133 Item 13 in Part 3 of Schedule 6 amends section 48A by repealing current subsections 48A(1) and (2) and substituting new subsections 48A(1) and (2) to:

- allow for circumstances in which a person whose life is insured under a contract of life insurance may be a third party beneficiary;
- ensure that a third party beneficiary who has a claim over money payable under the contract of life insurance may bring an action against the insurer in respect of the claim without the intervention of the policyholder; and
- ensure that the third party beneficiary is capable of giving a valid discharge to the insurer in relation to the insurer's obligations in respect of the claim.

Application

2.134 By operation of item 14 in Part 3 of Schedule 6, the amendment in Part 3 of Schedule 6 applies to a contract of life insurance that was originally entered into after the commencement of item 14.

2.135 If a contract of life insurance that was originally entered into before the commencement of item 14 is varied after that commencement to increase a sum insured under the contract, or to increase the number of life insureds under the contract, or to provide one or more additional kinds of cover, then the contract is treated, to the extent of the variation, as if it had been originally entered into after the commencement of item 14, and the amendment made by item 13 in Part 3 of Schedule 6 applies to the contract to the extent of the variation.

2.136 By operation of clause 2, item 14 in Part 3 of Schedule 6 commences at the end of the period of 12 months beginning on the day the Act receives the Royal Assent.

Part 4 — Rights of third party to recover against insurers

2.137 Section 51 of the IC Act deals with the rights of third parties to recover directly against an insurer in circumstances where the insured under a contract of liability insurance is liable in damages to the third party. The section provides that, where an insured has died or cannot be found, the third party may bring an action against the insurer directly.

2.138 Items 15, 16 and 17 in Part 4 of Schedule 6 expand section 51 so that it not only covers liability of an insured but also liability of a third party beneficiary.

Application

2.139 By operation of item 18, the amendments in Part 4 of Schedule 6 apply to a contract of liability insurance originally entered into after the commencement of item 18. The amendments also apply to a contract of liability insurance that was originally entered into before the commencement of item 18 and is renewed after that commencement.

2.140 By operation of clause 2, item 18 in Part 4 of Schedule 6 commences on the day after the end of the period of 12 months beginning on the day the Act receives the Royal Assent.

Part 5 — Representative actions by ASIC on behalf of third party beneficiaries

2.141 Section 55A of the IC Act permits ASIC, if it considers it in to be the public interest, to bring or continue actions against insurers on behalf of one or more insureds in relation to certain breaches by the insurer of the IC Act.

2.142 Items 19 to 24 of Part 5 of Schedule 6 make several amendments to section 55A to extend ASIC's powers to cover bringing or continuing actions against insurers on behalf of third party beneficiaries as well as insureds.

Application

2.143 By operation of item 25, the amendments in Part 5 of Schedule 6 apply to contracts of insurance whether originally entered into before or after the commencement of item 25.

2.144 By operation of clause 2, item 25 in Part 5 of Schedule 6 commences on the day the Act receives the Royal Assent.

Part 6 — Non-disclosure or misrepresentation by members of group life insurance schemes

2.145 Insurers normally have a remedy for non-disclosures and misrepresentations made by insureds only prior to the time the contract was entered into. However, in the case of group contracts of life insurance that are taken out by, for example, superannuation trustees for the benefit of all the scheme members, the contract date will often pre-date the joining of the scheme by fund members. As a consequence, an insurer would ordinarily have no remedy for non-disclosure and misrepresentation in relation to members who join a group scheme and receive cover under the relevant contract of life insurance after the contract date.

2.146 To deal with this situation, current section 32 of the IC Act provides that non-disclosures or misrepresentations made in respect of scheme members of superannuation and retirement schemes are treated as though the contract were an individual contract of life insurance that was entered into at the time when the proposed member joined the scheme.

2.147 In some circumstances, individuals will join a superannuation scheme but there will be some delay before life insurance cover they acquire as part of joining that scheme is commenced. For example, a new employee may join a superannuation scheme and superannuation contributions may be made on their behalf, but before the insurer provides life insurance cover, that employee must undergo a medical examination and/or answer questions about their health.

2.148 In those circumstances, the existing section 32 would still deny the insurer a remedy if non-disclosure or misrepresentation occurred during the interim period, because under current paragraph 32(b), the contract is taken to be entered into when the member joined the scheme.

2.149 Replacement section 32 in item 34 in Part 6 of Schedule 6 addresses this difficulty by providing that, where there is a delay from the time of joining the scheme until the time that cover is actually effected, the relevant contract of life insurance is taken to have commenced (that is, to be ‘entered into’) at the time the proposed life insured became a life insured under the scheme, in other words, at the time the life insurance cover under the scheme took effect in relation to the member concerned.

2.150 There are, in addition to ‘blanket’ contracts of life insurance taken out in connection with a superannuation scheme, other circumstances in which life insurance is taken out for a group of people, many of whom may become eligible for cover after the contract date. For example, contracts of life insurance for groups of people linked by a common factor such as employees of a company, or a scheme unrelated to employment such as membership of a health insurance scheme that offers members optional life insurance cover. Those other contracts also present a difficulty with the availability of insurer remedies for non-disclosure and misrepresentation.

2.151 A broader term is to be introduced for the purposes of the new section 32, namely, a ‘group life contract’, which is defined to mean a contract of life insurance that is maintained for the purpose of a superannuation or retirement scheme, or another scheme (including one not related to employment). This definition is inserted into subsection 11(1) by item 27.

2.152 The term ‘blanket superannuation contract’ in subsection 4(2) of the IC Act is replaced by item 2 with the expression ‘superannuation contract (other than an individual superannuation contract)’, and items 29 to 31 make some consequential changes to subsection 11(4).

2.153 Items 28, 32 and 33 change the phrase ‘superannuation or retirement scheme’ to ‘superannuation, retirement or other group life scheme’ in paragraph (b) of the definition of ‘proposal form’ in subsection 11(1) and in paragraphs 23(a) and 26(3)(a). This change enlarges the scope of operation of those provisions to encompass other types of group life schemes.

2.154 Item 35 corrects a typographical error in section 32A.

Application

2.155 By item 36 in Part 6 of Schedule 6, the amendments relating to replacement of the term ‘blanket superannuation contract’ by items 26, 29, 30 and 31 apply to a contract of life insurance whether originally entered into prior to, or subsequent to, the commencement of item 36. The

amendment to correct an error in 32A also applies to contracts entered into before or after commencement of item 36.

2.156 The remainder of the amendments in Part 6 apply to a contract of life insurance entered into after commencement of item 36 in Part 6 of Schedule 6.

2.157 Where a contract of life insurance that was originally entered into before the commencement of item 36 in Part 6 of Schedule 6 is varied after that commencement to increase a sum insured under the contract, or to increase the number of life insureds under the contract, or to provide one or more additional kinds of cover, then the contract is treated, to the extent of the variation, as if it had been originally entered into after the commencement of item 36, and the amendments made by items 27, 28 and 32 to 34 apply to the contract to the extent of the variation.

2.158 By operation of clause 2, Part 6 of Schedule 6 commences on the day after the end of the period of 12 months beginning on the day the Act receives the Royal Assent.

Schedule 7 — Subrogation

2.159 In the case of indemnity insurance, unless excluded by the terms of the contract, there is a right for an insurer to bring an action in the name of the insured (that is, the insurer is subrogated to the rights and remedies of the insured in respect of the subject matter insured) to pursue any claims the insured may have against third parties which have contributed to a loss. So if, for example, an insurer pays a claim to an insured arising from a motor vehicle collision, the insurer may, in the name of the insured, pursue actions against the person who caused the collision.

2.160 The amount recovered from the third party is often not equal to the amount the insurer has paid to the insured in respect of the loss. The costs of the action, and any difference between the amount of the loss and the amount insured, must also be considered when deciding to whom any recovered moneys should be paid.

2.161 Section 67 of the IC Act provides rules for how moneys recovered from a third party by an insurer under a right of subrogation should be divided between the insurer and the insured. The Review Panel listed a number of criticisms of section 67 in its review.

2.162 To address some of the difficulties experienced with the existing section 67, item 2 of Schedule 7 introduces a replacement section 67 containing rules that are intended to provide for the division of any

proceeds from a recovery action. This provision is based on the following principles.

- First, the party taking the recovery action should be entitled to reimbursement for the administrative and legal costs of that action from any moneys recovered. If both parties contribute, they both should be reimbursed (see new subsection 67(4)), or share the reimbursement pro rata if there is insufficient recovered money to reimburse both in full (see new subsection 67(5)).
- Secondly, there are three possibilities for distribution of remaining sums depending on who has funded the recovery action.
 - (a) If the insurer funds the recovery action pursuant to its rights of subrogation, it is entitled to an amount equal to the amount that it has paid to the insured under the contract of insurance. The insured is then entitled to any further amount necessary for it to ultimately recover from the insurer under the contract of insurance or the third party in the recovery action, or both in combination, the full amount of its loss (not just the measure of indemnity under the policy). This entitlement does not diminish the insured's right to receive payment under the policy in a prompt manner in accordance with the terms of the contract and the insurer's obligation to pay promptly, subject to any contrary agreement between the parties (see new subsection 67(2)).
 - (b) If the insured funds the recovery action, the order in the preceding paragraph is reversed. The insured is entitled to retain an amount so that the total that it receives from the recovery action and under the policy is equal to its total loss. The insurer is entitled at this point to an amount equal to the amount that it has paid to the insured under the insurance contract (see new subsection 67(3)).
 - (c) If the action is funded jointly by both the insurer and insured, they are both entitled to the same amounts as referred to in (a) and (b) above pro rata if there are insufficient funds to reimburse them in full (see new subsection 67(5)).
- Thirdly, any *excess* or windfall recovery is then to be distributed to both parties in the same proportions as they contributed to the administrative and legal costs of the

recovery action (see new subsection 67(7)). Through this process, the party (or parties) that bore most of the cost and risk of the recovery action should receive the benefit of the windfall. Most commonly this would be the insurer — but the insurer only gets the benefit after the insured has received full recovery for all its losses, because the insured would have been entitled to these losses as damages from the third party, whether or not there was any insurance in place.

- Finally, any separate or identifiable component in respect of interest should be divided fairly between the parties, having regard to the amounts that each has recovered and the periods of time for which each party lost the use of their funds.

2.163 The Review Panel had also recommended, for the purposes of the new section 67, that third party beneficiaries should be treated as insureds and this is the effect of item 1 of Schedule 7. Accordingly, the same principles of subrogation apply whether the person being indemnified is the insured party or a third party beneficiary to whom the indemnity cover extends.

2.164 New subsection 67(9) provides that the rights of the insurer and insured (or third party beneficiary) under section 67 may be modified by the terms of the relevant insurance contract.

Application

2.165 By operation of item 3 of Schedule 7 and clause 2, the amendments made by Schedule 7 apply to a contract of general insurance that was originally entered into after the commencement of item 3. Schedule 7 also applies to a contract of general insurance that was originally entered into before the commencement of item 3 of Schedule 7, and is renewed after that commencement.

2.166 By operation of clause 2, item 3 of Schedule 7 commences on the day after the end of the period of 6 months beginning on the day the Act receives the Royal Assent.