

Key Facts Sheet: Home Building and Home Contents Insurance Policies

Discussion Paper
February 2012

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Manager
Communications
The Treasury
Langton Crescent Parkes ACT 2600
Email: medialiasion@treasury.gov.au

Consultation Process

Request for feedback and comments

The Government is seeking your feedback and comments on the proposed regulations for the Key Facts Sheet as provided for by Division 4 of Part IV of the *Insurance Contracts Act 1984*.

Specific focus questions have been included on which feedback is sought. While submissions may be lodged electronically, by post or by facsimile, electronic lodgement is preferred.

All information (including name and address details) contained in submissions will be made available to the public on the Treasury website unless respondents indicate that they would like all or part of their submission to remain in confidence. Automatically generated confidentiality statements in emails do not suffice for this purpose. Respondents who would like part of their submission to remain in confidence should provide this information marked as such in a separate attachment. A request made under the *Freedom of Information Act 1982* to make available a submission marked 'confidential' will be determined in accordance with that Act.

Closing date for submissions: 23 March 2012

Email: icareview@treasury.gov.au

Mail: The Manager
Financial Services Unit
The Treasury
Langton Crescent
PARKES ACT 2600

Enquiries: Enquiries can be initially directed to Michelle Calder

Phone: 02 6263 2084

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FOREWORD



Too many people are confused by lengthy insurance contracts and product disclosure statements. In many instances, these documents are dozens of pages long and are written in dense legalese.

This problem was highlighted in the 2010/11 natural disasters that struck Australia, where many people discovered after major events that they weren't covered for risks that they thought they were. It is tragic that following such devastation, the difficulties experienced by people was often compounded by not understanding their insurance contracts, and the devastating realisation for some people that they were significantly underinsured.

On Christmas day many Australians faced significant storm events, which brought huge hailstones, torrential rain, flash flooding and even a tornado to parts of metropolitan Melbourne. Far from being unusual, these storm events became the eighth catastrophe declared by the general insurance industry in 2011, including the significant floods of 2010/11 and cyclone Yasi.

This confusion is not limited to natural disasters. Many people find insurance documentation daunting more generally and would be hard pressed to clearly explain the scope of their coverage. Clearly this is not an acceptable situation given the critical role that insurance plays in protecting people from risk.

That is why this Government is committed to implementing a mandatory one page Key Facts Sheet. The Key Facts Sheet will be a one page summary that clearly sets out what is covered and what is not covered. It will both improve people's understanding of their cover and make it easier to compare policies.

I am very pleased to release this discussion paper containing proposals for regulations to outline details of Key Facts Sheets for Home Building and Home Contents insurance policies. The purpose of this discussion paper is to seek community feedback on the content, format, structure and provision of a Key Facts Sheet, to ensure it achieves its intended purpose.

This discussion paper is an important step in assisting consumers to understand the basic terms of their Home Building and Home Contents insurance policies, including the nature of cover and any key exclusions.

I encourage you to participate in this consultation and provide your views on the proposals outlined in this paper.

The Hon Bill Shorten MP

Minister for Employment and Workplace Relations, and Minister for Financial Services and Superannuation

GLOSSARY AND ABBREVIATIONS

Term	Definition
ASIC	Australian Securities and Investments Commission
ICA	<i>Insurance Contracts Act 1984</i>
ICR	<i>Insurance Contracts Regulations 1985</i>
HBHC	Home Building and Home Contents
KFS	Key Facts Sheet
NDR	National Disaster Insurance Review
PDS	Product Disclosure Statement
RFI	Reforming Flood Insurance: Clearing the waters
The 2011 Bill	<i>Insurance Contracts Amendments Bill 2011</i>
The Corporations Act	<i>Corporations Act 2001</i>

1 KEY FACT SHEET

1.1 PURPOSE

1. A Key Fact Sheet (KFS) is a one page document which summaries key information about a Home Building and Home Contents (combined and individual) (HBHC) insurance policy. It will allow consumers to quickly and easily check the basic terms of the insurance policy, including the nature of cover and any key exclusions. The introduction of KFSs will also help consumers to compare the features of various insurance policies and select appropriate insurance products for their needs.
2. The purpose of this discussion paper is to seek community feedback on the content, format, structure and provision of a KFS for HBHC insurance policies. This community feedback will allow the Government to develop a prototype KFS that will be consumer tested. Once consumer testing is finalised, regulations will be made to give effect to the KFS.

1.2 BACKGROUND

1.2.1 Recent natural disasters

3. In recent years, there has been a significant increase in the number of natural disasters. In 2009, the Black Saturday Bushfires spread across over 450,000 hectares in Victoria. In 2010-2011, areas of Queensland, New South Wales and Victoria all experienced severe flooding. Queensland also suffered the effects of Cyclone Yasi and on Christmas day 2011 metropolitan Melbourne faced huge hailstones, torrential rain, flash flooding and even a tornado.
4. A substantial proportion of the cost of losses resulting from natural disasters is met by insurance. On 28 June 2011, the Insurance Council of Australia (ICA) indicated that, in relation to the Queensland floods and Cyclone Yasi, in excess of 99 per cent of claims had been assessed and determined. ICA member companies had received an estimated \$3.64 billion in claims, with 68,300 claims due to Cyclone Yasi, and 56,200 due to the 2011 Queensland flood event.
5. On 21 December prior to the Christmas day storms the ICA¹ released the final catastrophe figures for 2011 indicating that for: the Queensland floods, 58,463 claims were made with an estimated cost of \$2.4 billion; Cyclone Yasi, 72,203 claims were made with an estimated cost of \$1.33 billion; the Perth bushfires, 410 claims were made with an estimated cost of \$35 million; the Victorian floods, 7952 claims were made with an estimated cost of \$122 million; the Victorian severe storms, 49,396 claims were made with an estimated cost of \$412.3 million; and the Margaret River bushfires, 392 claims were made with an estimated cost of \$52.3 million.
6. These catastrophic events highlight the importance of insurance and making sure that individuals, families, communities and governments have effective insurance cover in place to guard against and recover from disasters.

¹ ICA media release "Cost of 2011's catastrophes passes \$4.3 billion as builders take a break" 21 December 2011

1.2.2 Reforming flood insurance: Clearing the waters

7. On 5 April 2011, as a first step in reforming flood insurance, the Hon Bill Shorten MP, Assistant Treasurer and Minister for Financial Services and Superannuation, released a consultation paper “Reforming flood insurance – Clearing the waters”. The consultation paper was released to engage the community on some particular suggestions for improving the regulatory framework for flood insurance and other aspects of Australia’s insurance market.
8. The consultation paper contained two key proposals designed to give consumers greater clarity about their insurance coverage, one of which was the introduction of a KFS, outlining the key information in relation to HBHC.
9. The consultation paper sought comments on a one page disclosure document (the KFS) which would allow consumers to quickly and easily check the basic terms of the insurance policy, including the nature of cover and any key exclusions.
10. The consultation paper highlighted a number of matters that should be included in a KFS. These matters included items such as the name of the policy, the type of the policy, what is and what is NOT covered under the policy. The consultation paper also contained a prototype of a KFS (Appendix A) and an additional option for the what is and what is NOT covered section of the KFS (Appendix B) in order to illustrate what the KFS may look like once its content had been finalised.
11. A significant number of submissions from industry groups and consumer advocates were received in response to the paper. The submissions indicated a broad level of support for the introduction of a KFS. However, many of submissions indicated that further consultation would be required in the development of the KFS.

1.2.3 The introduction of the *Insurance Contracts Amendment Bill 2011*

12. On 23 November 2011, the Government introduced the *Insurance Contracts Amendment Bill 2011* (the 2011 Bill) into Parliament. The 2011 Bill introduces a legislative framework into the *Insurance Contracts Act 1984* (ICA) to enable regulations to outline details of the KFS for HBHC insurance policies.

2 PRESCRIBING THE KEY FACT SHEET

2.1 CONTENT

2.1.1 The name of the policy

13. The name of an insurance policy is considered to be an essential feature of that policy, be it a Home Building policy, a Home Contents policy or a HBHC policy. A separate KFS will be required for each policy.

2.1.2 Type of policy

14. To provide insurance cover to meet a wider range of consumer needs, insurers offer a number of different types of cover in their policies. Three common types of policies are:

Sum-Insured Policies

- Sum-insured policies give consumers the flexibility to select the maximum available payout for loss in respect of the home building or home contents.

While this may have the benefit of reducing insurance premiums (as a low maximum payout may be selected), the ability for an insured to set their own maximum payout may result in underinsurance if a significant insurance event, such as a flood, occurs. It can also be difficult for consumers to properly estimate their potential maximum losses as they lack the tools and expertise to make this determination.

Sum-Insured Policies plus Margin

- Some insurance policies also offer an additional level of payout amount above the maximum payout amount in relation to the sum-insured selected by consumers (this may be an optional or mandatory feature of the policy). This additional payout amount is usually between 10 and 25 per cent. With the provision of this additional payout amount, consumers are less likely to face the adverse consequences of underinsurance (although, if consumers select a low maximum payout, underinsurance may still occur). However, we note that there has been a tendency for building costs to rise after natural disasters by more than this additional amount, due to trade person and material shortages.

Total Replacement Policies

- Total replacement policies are also available for home buildings. These policies require consumers to provide information regarding their home so that the insurer can estimate the home's value. Total replacement policies provide for the full replacement of the home building in the event of a significant insurance event, thus effectively removing the possibility of underinsurance.

15. The differences in the cover provided in relation to different types of policy tend only to be recognised by consumers when a significant insurance event occurs that results in extensive damage or total loss. When these events/situations occur, the differences between the different policy types become apparent. As a result, some consumers are significantly underinsured, having chosen an insurance policy with an inappropriate type of cover, even where rebuilding costs have been correctly estimated.
16. Submissions to the consultation paper indicated that due to the diversity within the HBHC insurance market and the length limitations of the KFS, information regarding the type of policy should be restricted to cover only the policy in question and not include potential policy types.
17. To ensure consumers are fully aware of the importance of choosing the appropriate type of policy for their needs, it is proposed that insurers will be required to specify on the KFS the type of policy being considered. In addition to specifying the type of policy the KFS will also be required to provide a description of the 'covered amount' in respect of the policy, explaining in more detail exactly the type of policy offered.
18. A generic description of the three main types of policy (sum-insured/sum-insured plus margin/total replacement) may also be included on the reverse side of the KFS to further increase consumer awareness of the other types of policies that are available.

Discussion Questions

- Are there practical difficulties in classifying insurance policies into the types of insurance policies outlined above? If so, how should the type of policy be outlined in the KFS?
- Are there any other major types/ classifications of insurance policies? If so are additional types of insurance policy descriptions required?
- Should a definitive explanation/ outline of the type of policy be on the front side of the KFS with general explanations of the different policy types provided on the reverse?
- Will including information on the type of policy increase costs for industry? If so, please elaborate and provide the magnitude of costs where possible.

2.1.3 What is covered

19. When consumers are considering HBHC insurance policies, they tend to only seek information on a few key areas of the policies. One of the most common areas where information is sought is on the insurance coverage of different policies. In particular consumers focus on determining what events are and are NOT actually covered under those policies. The importance of understanding what is actually covered by particular policies was recognised in the proposal outlined in the consultation paper and reinforced in the submissions received in response to the paper.
20. When discussing the possible content of the “what is covered” section, the consultation paper indicated that it would be possible to prescribe a ‘minimum list’ or a standardised list of covered events that should be referred to. Submissions received reinforced this idea, with a significant number of respondents indicating that the standard cover regulations provided under the Insurance Contracts Regulations (ICR) would be a logical starting point. The submissions also indicated that further consultation would be required in order to establish the events to be included in the final “what is covered” section of the KFS.
21. To increase comparability of insurance policies, the consultation paper also suggested that the order of covered events contained in the “what is covered” section be prescribed, ensuring consistency across all KFSs. This idea was also positively received in submissions, however, consistent with consideration of the events to be included in the “what is covered” section, further consultation was sought in respect of this suggestion.

Standard Cover

22. The standard cover regime in Part V of the ICA ensures that any exclusions and limitations that may apply in relation to particular insurance contracts are brought to the attention of insureds prior to any contract being entered into.
23. Section 35 of the ICA requires an insurer to bring to the attention of an insured, before the contract is entered into, the terms of the insurance contract that differ from the standard terms of a prescribed contract. The Explanatory Memorandum to the *Insurance Contracts Bill 1984* when discussing standard cover stated that:

“Where an insured makes a claim under a prescribed contract (i.e. a contract to which the standard cover provisions apply) and that claim is in respect of loss arising from an event prescribed in the [Insurance

Contracts Regulations], the insurer must pay [the insured] the minimum amount specified in the regulations. This is so even where the amount of the insurance cover is not provided by the contract is less than the minimum amount, or insurance cover is not provided by the contract at all [section 31(1)] unless the insurer proves that:

- *Before the contract was entered into [the insurer] clearly informed the insured in writing that less cover (or no cover) was provided; or*
- *The insured knew, or a reasonable person in the circumstances could be expected to have known that less cover, or no cover as the case may be, was provided [sec35(2)]”²*

24. HBHC insurance policies, to which the KFS requirements will apply, are both contracts to which the standard cover provisions apply.

25. The regulations which outline prescribed events are a good starting point for considering the content of the KFS.

Standard Cover Regulations for both Home building and Home contents insurance

The prescribed events for both Home building and Home contents insurance include:

- The destruction of, or damage occurring to, the home building on the site, being destruction or damage that is caused by or results from **and** the destruction of, or damage occurring to, the contents of a residential building which is specified in the contracts, at the time when they are in the residential building or on the site of the residential building, being destruction or damage that is caused by or results from:
 - Fire or explosion;
 - Lighting or thunderbolt;
 - Earthquake;
 - Theft, burglary or housebreaking or an attempt to commit theft, burglary or housebreaking;
 - A deliberate or intentional act;
 - Bursting, leaking, discharging or overflowing or fixed apparatus, fixed tanks or fixed pipes used to hold or carry liquid of any kind;
 - Riot or civil commotion;
 - An action of a person acting maliciously;
 - Impact by or arising out of the use of a vehicle (including an aircraft or water-borne craft);
 - Impact by:
 - (a) Space debris or debris from an aircraft, rocket or satellite;
 - (b) An animal (other than an animal kept on the site or a domestic animal);

² Insurance Contracts Bill 1984, Explanatory Memorandum, page 53-54

- (c) A falling tree or part of a tree; or
- (d) A television or radio aerial that has broken or collapsed;
- Storm, tempest, flood, the action of the sea, high water, tsunami, erosion or land slide or subsidence;

Applicable only to Home building insurance

- Accidental damage that is breakage of any fixed glass, fixed shower base, fixed basin, fixed sink, fixed bath, fixed lavatory pan or fixed cistern;
- Loss by theft, burglary or housebreaking;
- The insured or member of the insured’s family ordinarily residing with the insured incurring the liability as owner or occupier of the home building to pay compensation or damages to some other person.

Applicable only to Home contents insurance

The prescribed events of Division 3 of the ICR include:

- Accidental damage that is breakage of glass forming part of an item of furniture (including fixed or unfixed glass table tops), at a time when it is in the residential building or on the site if the residential building (only applicable to Home contents insurance);
- Loss by theft, burglary or housebreaking of contents while in the residential building on the site;
- Where:
 - The insured is a tenant or lessee of the residential building; or
 - The residential building is a unit (however described) created by the subdivision of strata (however described) in a building and the insured is the owner of the unit;
- The insured or a member of the insured’s family ordinarily residing with the insured incurring a liability as occupier of the home building to pay compensation or damages to some other person.

26. While the prescribed standard cover events provide an appropriate starting point for the content of the “what is covered” section, there is a limit to the number of events that can be included in a one page KFS. Therefore, it is essential that the prescribed events that are most beneficial for effective consumer decision making are covered. As such, it is proposed that events listed on the KFS be restricted to those events that lead to the most confusion or have the most significant financial impact.

Discussion Questions

- Of the prescribed events in the standard cover regime, which events (if any) lead to consumer confusion or lack of understanding about what is covered by the policy? What evidence is there that this confusion leads to adverse outcomes? Will the inclusion of these events (if any) in the KFS reduce the level of consumer confusion?
- Of the prescribed events in the standard cover regime, which events, if they occur, are most likely to have a significant financial impact on consumers? Is there any evidence that the inclusion of these events in the KFS will reduce the potential for significant financial to occur?
- In general, what standard cover events should be included in the KFS? What standard cover events should not be included in the KFS?
- Are there any other events outside standard cover that should be included?
- Will costs (monetary and non-monetary) for industry increase with an increase number of standard cover events? If so, please elaborate and provide the magnitude of costs where possible.

Natural Disaster Events

27. In the National Disaster Insurance Review (NDIR) conducted last year into disaster insurance in Australia, concerns were raised about the current disclosure regime and its failure to sufficiently inform consumers of the relevant terms and conditions of insurance policies in relation to natural disaster events. In this regard it was reported that many policy holders affected by the 2011 floods in Queensland discovered, reportedly for the first time, that their HBHC insurance policies would not fully cover them for flood damage.
28. In this context, the NDIR's report (released on 4 November 2011) endorsed the introduction of a KFS and indicated that the KFS should list the natural disaster events, identified as events to which standard cover in the ICR applied (recommendation 33).
29. The standard cover regime currently identifies the following natural disaster events: fire; earthquake; flood; tsunami and land slide.

Discussion Questions

- Should all of the natural disaster events that are considered to be prescribed events in the standard cover regime be included in the KFS? If not which natural disaster events should not be included?
- Are there any other natural disasters that should be included?
- Will the inclusion of the natural disaster events in the KFS increase costs for industry? If so, please elaborate and provide the magnitude of costs where possible.

2.1.4 What is NOT covered

30. As noted, the insurance coverage of different policies is an area of key interest to consumers. In this regard, consumers place a considerable focus on exclusions that may apply in relation to their insurance policies; that is, what events are not covered.
31. When looking at the potential content of the “what is NOT covered” section of the KFS the consultation paper indicated that the “what is NOT covered” list should be in essence the reverse of the “what is covered” section.
32. However, to ensure appropriate consumer outcomes are achieved, further consideration and consultation regarding the content of the “what is NOT covered” section is required.
33. In this regard, information regarding exemptions provided in the ICR in relation to standard cover and information about the prescribed standard cover events not covered in the “what is covered” area must be taken into consideration.
34. Taking this approach provides consumers with a comprehensive understanding of the key information regarding the status of the exceptions and conditions of the particular HBHC insurance policy/ policies under consideration.

Exemptions provided in relation to cover insurance policies

35. Currently under the ICR, standard cover insurance contracts for Home building insurance and Home contents insurance have a number of exemptions which include:
 - depreciation;
 - wear and tear, rust or corrosion;
 - the action of insects or vermin;
 - destruction of, or damage occurring to:
 - an electrical machine or apparatus as a result of the electric current in it; or
 - any property as a result of it undergoing a process necessarily involving the application of heat

Applicable only to Home building insurance

- destruction or damage, or the incurring of a liability in respect to the insured or member of the insured’s family ordinarily residing with the insured incurring the

liability as owner or occupier of the home building to pay compensation or damages for home building insurance as a result of:

- the expropriation of the home building;
- war or warlike activities;
- the use, existence or escape of nuclear weapons material, or ionizing radiation from, or contamination by radioactivity from, any nuclear fuel or nuclear waste from the combustion of nuclear fuel;
- the use of the home building for the purposes of a business, trade or profession; or
- tree-logging or felling by the insured or a person acting with the express or implied consent of the insured; or
- or intentionally incurred, by:
 - (1) the insured; or
 - (2) a member of the insured's family ordinarily residing with the insured; or
 - (3) a person acting with the express or implied consent of any of them;
- where the home building is unoccupied and has been unoccupied for a continuous period of more than 60 days — destruction or damage occurring otherwise than as mentioned in subparagraph by lightning or thunderbolt: or earthquake; or theft, burglary or housebreaking or an attempt to commit theft burglary or house breaking; or riot or civil commotion; an action of a person acting maliciously; impact by or arising out of the use of a vehicle (including an aircraft or water-borne craft); or impact by space debris or debris from an aircraft, a rocket or satellite an animal (other than an animal kept on the site or a domestic animal) a falling tree, or part of a tree, or a television or radio aerial that has broken or collapsed; or a storm, tempest, flood, the action of the sea, high water, tsunami, erosion or land slide or subsidence, or the incurring of liability in respect to the insured or member of the insured's family ordinarily residing with the insured incurring the liability as owner or occupier of the home building to pay compensation or damages to some other person;
- destruction of, or damage occurring to:
 - a free-standing or retaining wall (whether or not part of the home building), or to a gate or fence, as a result of a storm or tempest;
- theft by a person ordinarily residing with the insured at the time of the theft;
- in the case of destruction or damage that is caused by or results from bursting, leaking, discharging or overflowing of fixed apparatus, fixed tanks or fixed pipes used to hold or carry liquid of any kind or impact by a television or radio aerial that has broken or collapsed — damage to the apparatus, tanks or pipes or the television or radio aerial, respectively;
- the incurring of a liability in respect to the insured or member of the insured's family ordinarily residing with the insured incurring the liability as owner or

occupier of the home building to pay compensation or damages for home building insurance:

- to the insured or a member of the insured's family ordinarily residing with the insured; or
- as a result of:
 - (1) the insured; or
 - (2) a member of the insured's family ordinarily residing with the insured; or
 - (3) a person acting with the express or implied consent of any of them, using a vehicle (including an aircraft or water-borne craft) on the site.

Applicable only to Home contents insurance

- destruction or damage, or the incurring of a liability where the insured is a tenant or lessee of the residential building; or the residential building is a unit (however described) created by the subdivision of strata (however described) in a building and the insured is the owner of the unit, as a result of:
 - the expropriation of the home building;
 - war or warlike activities;
 - the use, existence or escape of nuclear weapons material, or ionizing radiation from, or contamination by radioactivity from, any nuclear fuel or nuclear waste from the combustion of nuclear fuel;
 - the use of the residential building for the purposes of a business, trade or profession; or
 - tree lopping or felling by the insured or a person acting with the express or implied consent of the insured;
- destruction or damage intentionally caused, or a liability where the insured is a tenant or lessee of the residential building; or the residential building is a unit (however described) created by the subdivision of strata (however described) in a building and the insured is the owner of the unit, intentionally incurred, by:
 - the insured; or
 - a member of the insured's family ordinarily residing with the insured; or
 - a person acting with the express or implied consent of any of them;
- where the residential building is unoccupied and has been unoccupied for a continuous period of more than 60 days — destruction or damage occurring otherwise than by lightning or thunderbolt; or earthquake; or theft, burglary or housebreaking or an attempt to commit theft burglary or house breaking; or riot or civil commotion; an action of a person acting maliciously; impact by or arising out of the use of a vehicle (including an aircraft or water-borne craft); or impact by space debris or debris from an aircraft, a rocket or satellite an animal (other than an animal kept on the site or a domestic animal) a falling tree, or part of a tree, or a television or radio aerial that has broken or collapsed; or a storm, tempest, flood, the action of the sea, high water, tsunami, erosion or

land slide or subsidence; or the incurring of liability where the insured is a tenant or lessee of the residential building; or the residential building is a unit (however described) created by the subdivision of strata (however described) in a building and the insured is the owner of the unit;

- accidental breakage of:
 - a television picture tube or screen;
 - the picture tube or screen of an electronic visual display unit;
 - a ceramic or glass cooking top of a stove;
 - glass in a picture frame, a radio set or a clock;
- theft by a person ordinarily residing with the insured at the time of the theft;
- in the case of destruction or damage that is caused by or results from bursting, leaking, discharging or overflowing of fixed apparatus, fixed tanks or fixed pipes used to hold or carry liquid of any kind or impact by a television or radio aerial that has broken or collapsed — damage to the apparatus, tanks or pipes or the television or radio aerial, respectively;
- the incurring of a liability where the insured is a tenant or lessee of the residential building; or the residential building is a unit (however described) created by the subdivision of strata (however described) in a building and the insured is the owner of the unit.
 - to the insured or a member of the insured's family ordinarily residing with the insured; or
 - as a result of:
 - (1) the insured; or
 - (2) a member of the insured's family ordinarily residing with the insured; or
 - (3) a person acting with the express or implied consent of any of them, using a vehicle (including an aircraft or water-borne craft) on the site.

Prescribed standard cover events not covered in the “what is covered” section

36. If the prescribed events used in the “what is covered” section, form the basis for the “what is NOT covered” section, insurers will be required to disclose any derogations from these events in accordance with the standard cover regime.
37. It must be noted that while the KFS may be seen to disclose any derogations from standard cover as required under section 35 of the ICA, in respect to the covered events, the KFS will not be able to be used as a way of satisfying the clearly inform requirements in the ICA as the KFS is only a guide outlining the key information on the insurance policy.

The proposed content of the what is NOT covered section

38. While using the approach outlined above to determine what should be included in the “what is NOT covered” section of the KFS may be more complex to establish, the potential benefits for both consumers and insurers is likely to outweigh this complexity. It is recognised that if this approach is taken, the prescribed standard cover events that are not covered in the “what is

covered” section would be required to be included and given the length restrictions, only those exceptions that are deemed to be critical being included.

Discussion Questions

- What exclusions should be included in the “what is NOT covered” section?
- Should the “what is NOT covered” section of the KFS only reflect the reverse of the “what is covered” section?
- Should the “what is NOT covered” section reflect only events in relation to those contained in standard cover or should it be extended to include parts of the standard cover exclusions?
- Will costs for industry increase with an increase number of excluded events and exemptions? If so, please elaborate.

2.1.5 Sub-limits and Excesses

39. To limit the financial liability associated with some types of insurance cover, a number of insurers have introduced one or more sub-limits (or caps) for events covered in their policies. Insurance policies may include sub-limits for insurance events such as flood and fire, which restrict the maximum payout if one of these events occurs. When policies contain sub-limits, the sub-limits are generally set at significantly lower amounts than either replacement or sum-insured values.

40. When looking at the issues surrounding sub-limits the NDIR stated that:

“While the provision of flood cover with a sub-limit may be better than no flood cover at all, the Review Panel considers that flood cover when included should be on the same basis as cover for other perils.”³

41. The rationale for this is that the community expects insurance to provide the same protection for the insured in the event of a natural disaster, whether it be storm, bushfire, earthquake or flood, and may not understand that a total loss may result in a lower payout, if caused by certain events.

42. Excesses are another way that insurers are able to limit the insurance coverage provided in their policies. In contrast to sub-limits, instead of restricting an insurer’s exposure to large claims when an insurance event occurs, excesses effectively reduce the number of small claims under policies.

43. The consultation paper proposed that where an excess is standard across all policies of that type, the actual excess could be printed on the KFS. However where policies enable excesses to be varied for individual policyholders, the KFS would need to contain a statement that refers consumers to the PDS.

44. When considering excesses, the NDIR indicated that many of the difficulties that arise in relation to policy exclusions apply where insurance policies contain high excesses.

45. This needs to be balanced against the benefits of sub-limits and excesses improving the affordability and accessibility of insurance.

46. In the recent consultation paper “Reforming Flood Insurance: Improving flood insurance availability and transparency” the issue of sub-limits and excesses was raised in the context of a

³ Natural Disaster Insurance Review “Inquiry into flood insurance and related matters” September 2011, page 34

proposal to provide mandatory flood cover, with the ability to opt out, for consumers purchasing HBHC insurance policies.

47. If the proposal to introduce mandatory flood cover, with the ability to opt out, is adopted the incidence of sub-limits may significantly increase in order for insurers to maintain affordability, although the use of sub-limits and excesses in relation to flood cover is the subject of a separate Government consultation.
48. To ensure consumers are fully aware of the relevant factors when considering the level and type of insurance cover they require, disclosure of key financial information such as excesses and sub-limits are considered to be essential.
49. It is proposed to include, where a policy contains one or more sub limits or excesses which may be selected by the consumer, a statement on the KFS indicating that the PDS should be read prior to entering into the policy.

PROPOSED WORDING OF THE STATEMENT REGARDING SUB LIMITS AND EXCESSES

The insurance contract to which this KFS applies contains one or more sub limits and/ or excesses. You should carefully read the product disclosure statement and the policy schedule of the insurance policy to which this KFS applies before entering into the policy.

50. In addition, if sub-limits or excesses apply consistently across a HBHC insurance policy irrespective of the circumstances of an insured, the amount of the sub limit or excess would be required to be listed in the KFS adjacent to the covered event contained in the “what is covered” section.

Discussion Questions

- Is it appropriate to include information on specific excesses in the KFS?
- Is it appropriate to include a statement in the KFS acknowledging that sub-limits/ excesses apply in relation to a HBHC insurance policy?
- Is the wording of the statement regarding sub-limits and excesses appropriate?
- What percentage of HBHC policies have excesses in respect of covered events?
- Is it appropriate to include information on specific sub-limits in the KFS or should sub-limits be required to be acknowledged on the KFS with a reference that more information should be obtained from the relevant PDS?
- What percentage of HBHC insurance policies contain sub-limits?
- Will the use of sub-limits increase if mandatory flood cover with opt-out is introduced?
- Will the inclusion of information on sub-limits and excesses increase costs for industry? If so, please elaborate and provide the magnitude of costs where possible.

2.1.6 Cooling off period

51. To provide consumers with protection after an insurance contract is entered into, insurers are required to provide a sufficient time period for consumers to consider the policy, and have an adequate cooling off period in respect to the policy.
52. The cooling off period provides consumers with the time to fully consider the suitability and appropriateness of the product free from any pressure or impulse. This allows consumers to evaluate all of the key information in relation to the particular policy and provides consumers with the ability to think over the advantages and disadvantages of a policy to ensure they have obtained the appropriate policy for their requirements.
53. The cooling off period is particularly important for insurance contracts entered into over the telephone. This is due to the application of section 69 of the ICA, which allows insurers, where it is not practical to provide relevant disclosure documentation at the time a contract is entered into, to provide it after an insurance contract is entered into.
54. When looking at consumer understanding of the cooling off period, it has been suggested that a significant number of consumers are unaware that a cooling off period exists in relation to insurance policies and that during this period they are able to cancel their policy at no cost during that period.
55. Insurers currently provide a number of different cooling off periods in relation to their products. A sample of HBHC insurance policies showed that cooling off periods ranged from 20 to 30 days.
56. It is vital that consumers understand the purpose of the cooling off period and it is proposed that the length of cooling off period be outlined in the KFS and be contained in a short statement outlining the purpose of the cooling off period.
57. The Corporations Act provides a cooling off period for the return of a financial product (which includes the taking out insurance) of 14 days.

58. PROPOSED WORDING OF THE STATEMENT ON THE COOLING OFF PERIOD

*A cooling off period of ** days applies in relation to this policy. The cooling off period allows you to cancel this policy.*

Discussion Questions

- Should the time period for the cooling off period be in the KFS?
- Is the wording of the cooling off period statement appropriate?
- Are there any practical concerns regarding the inclusion of a section providing consumers with a time period of the cooling off period on the front of the KFS with an explanation on the reverse side?
- Will the inclusion of the cooling off period (including a statement) increase costs for industry? If so, please elaborate and provide the magnitude of costs where possible.

2.1.7 Warnings/ statements

How to use the KFS

59. The objective of the KFS is to provide consumers with the key information on their HBHC insurance policies. This will enable consumers to compare and access different policies in order to make appropriate insurance decisions.
60. To maximise the effectiveness of the KFS it is considered essential that a short statement outlining how it is to be used and its legal effect should be contained in the KFS. The importance of the inclusion of a statement on how to use the KFS was also recognised in a significant number of the submissions received in respect of the RFI consultation paper.
61. The KFS is not intended to be a document to be used in isolation or as an alternative to the current disclosure documentation required under the ICA and the Corporations Act. The KFS does not have the same legal effect as the current disclosure documents required under these Acts.
62. On the basis that the KFS is in essence merely a guide containing key information pertaining to a HBHC, KFSs should contain a statement indicating its purpose and its legal effect.
63. In addition, the statement could include wording to encourage consumers to read the full PDS.

THE PROPOSED WORDING FOR THE “HOW TO USE THE KFS” STATEMENT

OPTION 1

*This Key Facts Sheet provides an outline of some of the key facts and information you should take into consideration prior to entering into this policy. This Key Facts Sheet may also be used to compare this policy with other similar policies to ensure your insurance needs are met. This Key Facts Sheet is **NOT** a comprehensive disclosure document and you should read this policy’s product disclosure statement before taking out the policy.*

OPTION 2

This KFS is to be used as an informative guide and does not contain all relevant information about this policy. The KFS is not a substitute for this policy's product disclosure statement and should not be used as such.

Discussion Questions

- Is a "How to use a KFS" statement required?
- Is the wording of the proposed "How to use a KFS statement" appropriate?
- Should additional information be included in the statement? If so, please elaborate.
- Will the inclusion of a "How to use a KFS statement" increase costs for industry? If so, please elaborate and provide the magnitude of costs where possible.

General consumer warning/Risk statement

64. The nature of insurance is such that consumers are usually unaware of the financial risks they face when entering into an insurance contract. Financial risks and adverse consumer outcomes are only fully recognised after a particular insurance event occurs, such as a flood or an earthquake.
65. In this regard, despite the standard cover regime applying to HBHC insurance contracts, significant differences in the level of insurance cover can arise when an insurance event occurs.
66. To make this clearer to consumers, it is proposed that a statement providing a general consumer warning/ risk statement be included in the KFS.

PROPOSED WORDING OF THE "GENERAL CONSUMER WARNING/ RISK STATEMENT"

Due to the nature of insurance contracts and their potential financial impacts, consideration should be given to the "what is covered" and "what is not covered" sections of this KFS to ensure that this policy covers your particular risks and needs.

Discussion Questions

- Is a "General consumer warning/ Risk statement" required?
- Is the wording of the proposed "General consumer warning/ Risk statement" appropriate?
- Should additional information be included in the statement? If so, please elaborate.
- Will the inclusion of a "General consumer warning/ Risk statement" increase costs for industry? If so, please elaborate and provide the magnitude of costs where possible.

Health warning

67. In NDIR's report into the insurance industry, the review panel recommended that the KFS should contain a health warning. This health warning would provide consumers with information on the potential risks that may arise in relation to insurance and the potential adverse outcomes that may arise as a result of them taking or failing to take particular actions in respect to their insurance decisions. It was considered that the health warning would further enhance the consumer understanding that will be provided in the KFS prescribed content.
68. A simple health warning for HBHC insurance policies could be as simple as those provided for other products and could also be provided verbally if the KFS could not be provided at the time an inquiry regarding the HBHC insurance policy is made.
69. NDIR's final report indicated that it would be appropriate for the insurer to provide the purchasers of home and contents policies with a health warning if their policies did not include full flood or full replacement cover.

PROPOSED WORDING OF THE HEALTH WARNING

The importance of making informed decisions regarding your insurance requirements should not be overlooked, the incidence of natural disasters and their potential financial impact can place you in significant financial hardship. It is strongly recommended that you read this KFS and the PDS and consider whether the cover is appropriate for you, and seek further information if required.

Discussion Questions

- Is a general health warning required? If so, where should it appear – front or reverse side of the KFS?
- Will a general health warning be beneficial for consumers when looking at particular policies?
- If a health warning is on the KFS, should the warning also focus on the potential risks for failing to secure appropriate insurance cover? Or the adverse effects of underinsurance?
- Will the inclusion of a health warning increase costs for industry? If so, please elaborate and provide the magnitude of costs where possible.

The Wayne Tank Principle

70. The Wayne Tank principle, as set down in *Wayne Tank & Pump Co Limited - v - Employers Liability Assurance Co⁴*, provides that:
- If there are two or more concurrent causes of damage in respect of a loss or damage to an insured's property and one of those concurrent events are excluded events in the insured's insurance policy, then the exclusion will still

⁴ Wayne Tank and Pump Co Ltd v. Employers Liability Assurance Corporation Ltd [1974] QB 57

apply such that the insurer will not have to indemnify the insured in respect of the loss or damage.

71. The potential adverse financial outcomes consumers may face as a result of the Wayne Tank principle have been raised as a potential area of concern. In order to address this concern it is proposed that the KFS will contain a short statement raising the potential application of the Wayne Tank principle and its potential effect.

PROPOSED STATEMENT REGARDING THE WAYNE TANK PRINCIPLE

In situations where there are two or more concurrent causes for damage to your property and one of the causes is excluded under this policy any claim made in respect of that damage may be excluded.

Discussion Questions

- Will consumers benefit from the inclusion of a statement outlining the application of the Wayne Tank principle? If not, why not?
- Is the wording of the statement regarding the Wayne Tank principle appropriate? If not, why not?
- If space is limited should the Wayne Tank principle be included?
- Will the inclusion of a statement outlining the Wayne Tank principle increase costs for industry? If so, please elaborate and provide the magnitude of costs where possible.

Additional informational statements suggested in submissions in the Reforming flood insurance: Clearing the waters consultation paper

72. The RFI consultation paper sought input from stakeholders on what other matters should/ could also be contained in the KFS. In response, submissions outlined a number of other matters for consideration for inclusion in the KFS. Most of the matters raised may be included in other areas of the KFS such as in the “How to use the KFS”, however a number of the other matters raised may warrant consideration and be included in the KFS. The matters raised in the submissions included:

- a warning that the KFS is for information only and is not a binding contract on either the insured or the insurer;
- a list of the key terms and concepts referred to in the KFS;
- information on claims processes;
- a statement covering the role of both internal and external dispute resolution processes and the role of the Financial Services Ombudsman;
- a statement that encourages consumers to fully consider all potential risks that may apply in relation to their insurance decisions;
- a statement warning that other exclusions and limitations may apply in relation to the relevant policy and that consumers should read the policy’s product disclosure statement in order to become fully aware of all of the exclusions and limitations that may apply; and

- a statement encouraging consumers to actively review their insurance decisions on an annual basis to ensure their insurance needs are still being met.

Other matters raised in the RFI consultation paper

73. Other matters were also raised in the consultation paper, including:

- a brief explanation of policy types (sum-insured/sum-insured plus margin/total replacement);
- a statement encouraging consumers to consider carefully whether the policy adequately covers the risks that are faced by their property;
- a statement encouraging consumers to consider other policies; and
- sources of additional relevant information (for example, relevant consumer websites).

74. While most of the submissions supported the inclusion of generic consumer information statements, the common theme across all submissions was that the KFS should be kept uncluttered and that these generic statements should only be included if they do not jeopardise the integrity of the KFS.

Discussion Questions

- Should any of the suggested statements be included on the reverse side of the KFS? If so, which statements do you consider to be most important?
- Are there any other matters to which a statement in the KFS would benefit consumers? If so, please elaborate?
- Will the inclusion of additional statements on the reverse side of the KFS increase costs for industry? If so, please elaborate and provide the magnitude of costs where possible.

2.2 STRUCTURE

75. As noted in paragraph 9, the RFI consultation paper contained a prototype of a KFS. For the purposes of developing the KFS, the KFS prototype will be taken as the starting point for discussion.

76. In relation to the structure of the KFS, the only restriction is keeping its length to a one A4 page sheet. It is intended that the KFS will contain the key information regarding the particular policy to which it applies and any other key consumer information, on the front, with some generic information contained on the reverse.

Discussion Questions

- While the final structure of the KFS will not be able to be finalised until the content has been settled, is the prototype contained in the “Reforming flood insurance: Clearing the waters” consultation an appropriate starting point?
- Are there any other feasible ways to structure the KFS outside those provided in the Reforming flood insurance: Clearing the waters” consultation paper? If so, please provide an example of alternative prototypes?

2.3 GENERAL FORMATTING

2.3.1 Font

77. To provide consistency across all KFS for HBHC insurance policies the font, to be used for headings, normal text and tables will be prescribed. It is considered that providing consistency in relation to the font used in the KFS is essential for reducing consumer confusion when viewing its contents.

2.3.2 Length

78. The length of the KFS will be kept to one page (A4), both front and back. The length of the KFS is in keeping with the fact that it is intended to be an informative guide to provide consumers with easy access to key information relating to HBHC insurance policies.

2.3.3 Positioning

79. The positioning of the information is essential to the effectiveness of the KFS. Key statements outlining the way in which the KFS should be used and the legal nature and effect of the KFS (in keeping with the prototype) should be placed at the top of the front page, just below factual information regarding who the insurance provider is, the name of the contract/ policy to which the KFS applies.

80. Logically, the type of cover the policy provides (sum-insured, replacement cover, etc.) as it relates directly to the level of financial cover should also be placed towards the top of the front page.

81. In relation to the other content of the KFS, the two key sections that are essential to the effectiveness of the KFS, “what is covered” and “what is NOT covered”, should also be in a prominent position.

2.3.4 Wording

82. In relation to the wording of the KFS, it is recognised that to reduce confusion and to ensure that the length requirement (as stated above) is able to be achieved, words and statements should be kept clear, concise and effective.

83. Consumer testing will assist in assessing the level of prescription of the wording of the KFS and to ensure that it is clear, concise and effective consumer testing will be required, however this will only be able to be undertaken after the actual content of the KFS is established.

84. It is expected that the “what is covered” and “what is NOT covered” sections and the wording of specific statements and other generic information concerning HBHC insurance policies will be prescribed in regulation.

Discussion Questions

- Are there any concerns with the proposed approach of prescribing the font requirements on the content (headings, tables, normal text etc.) of the KFS?
- What size should the font for the content of the KFS be? Should it be consistent with other disclosure documents?
- Are there any practical concerns with restricting the KFS to a one A4 page format (both front and reverse sides)?
- Is it appropriate for all of the content of the KFS to be prescribed or should the regulation only provide guidance regarding the wording of some sections of the KFS?

2.4 PROVISION

2.4.1 When the KFS is required to be provided

85. To ensure consumers are able to benefit from the KFS, the KFS should be available when they are making decisions about their insurance cover. To achieve this insurers are required to provide consumers with a KFS when a consumer inquires about a particular policy.
86. While the KFS is required to be provided when a consumer makes an inquiry, it is recognised that there may be a number of situations where it is inappropriate or ineffective to do so. In the Explanatory Memorandum to the 2011 Bill, the following situations were raised as situations where the provision of a KFS would not be required:
- where the insurer has already provided the consumer with a KFS for a particular HBHC insurance contract and the new KFS would be the same (except for its date);
 - where the insurer reasonably believes that another person has already provided the consumer with a KFS, and the new KFS would be the same (except for its date); and
 - where the consumer has indicated that they do not wish to have a KFS provided in relation the HBHC insurance contract that they are seeking information on.
87. It is proposed to provide an exemption in the regulations for the requirement to provide a KFS on inquiry in the situations as set out above.

Discussion Questions

- Are the situations where a KFS is not required to be provided as outlined above appropriate?
- Are there any other situations where a KFS should not be required to be provided be included? If so, please elaborate.
- How will consumers be affected if the scope of any potential exemptions from the requirement for insurers to provide a KFS is wider than those outlined above?
- If no exemptions for the provision of a KFS are provided in the regulation, what will be the cost implications for insurers?

Delays in the provision of a KFS

88. Section 69 of the ICA currently allows insurers to provide information within 14 days after the day a contract is entered into when it is not practicable for the information to be provided at the time. In situations where it is not possible to provide a consumer with a KFS at the time of inquiry, insurers will not be able to rely on section 69 of the ICA. However, as discussed in the Explanatory Memorandum to the 2011 Bill, it is proposed that regulations will be introduced to provide insurers with the ability to defer the provision of a KFS in circumstances where it is not possible to provide it at the time of inquiry.
89. While it was considered appropriate to allow the regulations to provide some flexibility in this area, the timing of the provision of a KFS is vital when considering the consumer's ability to use the KFS as a way of comparing policies.
90. In this regard, delays in the provision of the KFS could deter or prevent consumers from making informed decisions about their insurance cover and result in consumers purchasing insurance policies that do not meet their needs.

Discussion Questions

- Does the timing of the provision of the KFS raise any practical concerns for insurers?
- Are there any circumstances where it is appropriate to allow for insurers to provide a KFS at a later date if it not possible to provide it at the time of inquiry?
- Should the issue of the quotation of HBHC insurance policies over the telephone be considered in the context of the provision of the KFS?
- Are there any cost impacts for insurers if the provision of a KFS is not able to be delayed? If so please elaborate and provide the magnitude of costs where possible.

2.4.2 Method

91. Under the ICA, insurers are not currently able to satisfy its notification requirements using methods of electronic communication. The ICA only allows written notifications to be provided to insureds personally or to their last known postal address. The KFS will continue to be able to be provided as currently allowed under the ICA. However, to reduce compliance

costs for industry and allow for greater access for consumers when making their insurance decisions, the provision of a KFS will also be able to be made electronically.

92. The ability for insurers to engage in electronic communication will allow insurers to provide a printable copy of the KFS on their websites and send the KFS (in electronic form) via email.

Discussion Questions

- Are there any practical or logistical issues regarding the proposed methods for which the KFS will be provided?
- Are there any cost implications in relation to the allowed methods for the provision of the KFS? If so, please elaborate and provide the magnitude of costs where possible.

2.5 FAILING TO COMPLY WITH THE REGULATIONS REGARDING KEY FACTS SHEET

93. To ensure the KFS achieves its policy intent, the 2011 Bill makes it an offence for an insurer to fail to comply with or engage in conduct that contravenes any requirement contained in the regulations in respect to the content, format, structure and provision of a KFS. An insurer will be subject to a criminal penalty of 150 penalty units if it commits the offence of failing to comply with the KFS regulations.

94. The offence and criminal penalty created in respect to KFSs was introduced to ensure that the disclosure to individual consumers receives the appropriate level of attention by insurers.

2.6 THE MONITORING AND ADMINISTRATION OF THE KFS

95. The Australian Securities and Investments Commission (ASIC) is responsible for the monitoring and administration of the ICA and will monitor compliance in relation the content, formatting and provision of KFSs.

2.7 IMPACTS /COSTS

96. It is recognised that the introduction of the KFS will increase compliance costs for industry. The increased compliance costs will be incurred in the establishment (statement development and legal costs), implementation (systems changes, website updates and front line staff training costs) and ongoing annual costs (printing and distribution costs) of the KFS.

97. The potential areas, where proposals outlined in this discussion paper may have a cost impact are those relating to the initial establishment and implementation costs of the KFS.

98. In this regard, the potential costs relating to the format, structure and, in particular, the content of the KFS should also be considered. However, it is important to note that the introduction of an effective and informative KFS will have benefits for the whole community and any cost will need to be assessed against these benefits.

Discussion Questions

- To what extent would different prototypes of the KFS impact on costs? Please provide the magnitude of costs if possible.
- Are there any aspects of the KFS where costs will be significantly increased as a result of proposals outlined in this discussion paper? If so, please elaborate and provide magnitude of costs where possible.
- Are there any areas of this discussion paper where industry cost should be considered/ recognised?

3 APPENDIX A

Proposed KFS in the “Reforming flood insurance: clearing the waters” consultation paper

CONSULTATION DRAFT

KEY FACTS ABOUT YOUR HOME INSURANCE POLICY

[Insurance provider logo]

Description of your home insurance policy			
Policy name	XYZ Home Building Classic		
Policy type	<input checked="" type="checkbox"/> Sum insured	<input type="checkbox"/> Sum insured plus margin	<input type="checkbox"/> Total replacement cost

How to use this statement
<p>You can use this statement to help you to find out quickly whether this insurance policy may suit you, and you can use it for comparing the features of this policy with other policies. It is a only short summary of key benefits and exclusions and before making a decision it is important that you read the full terms and conditions in the XYZ Home Building Classic Product Disclosure Statement which can be obtained from www.insurance.xyz or by telephoning us on XXXX.</p>

What is covered	What is NOT covered
Fire: eg damage from bushfire or fire caused by electrical fault	Damage from ash or soot if there is no fire in your home
Explosion	
Theft or attempted theft	
Stormwater/rainfall runoff	
Flood	Tsunami/actions of the sea
Impact	
Riot	
Occupier's liability	
	Other: <ul style="list-style-type: none"> landscaping, plants cars, boats

Covered amount: This policy is a 'sum insured' policy. The policy will only cover you up to fixed limits, agreed by you. You should ensure that the limits are adequate to compensate you for the losses you may have. For further information see [reference to tools to estimate the value to insure].

Need to consider risks: There may be risks such as flood, bushfire, land slippage in the area where the insured property is located. You should consider carefully whether this policy provides you with the cover you require for those risks.

Cooling Off: If you are not happy with your insurance cover, and have not made a claim, we will cancel and refund your premium in full within [XX] days of purchase.

Excess: An excess may be payable if a claim is made. The standard excess is \$XX [but this may be varied]. Please see the XYZ Home Building Classic Product Disclosure Statement [at page/paragraph XX].

Optional Cover: For an additional premium amount, we may insure items that are not standard. To find out about a range of our Optional benefits, please refer to the XYZ Home Building Classic Product Disclosure Statement which can be obtained from our website www.insurance.xyz or by telephoning us on XXXX.

CONSULTATION DRAFT

4 APPENDIX B

Possible alternative what is and what is not covered section

Event/risk	Is it covered?	Main limitations/exclusions
Fire or explosion	<input checked="" type="checkbox"/>	Damage from ash or soot if there is no fire in your home is excluded
Stormwater/rainfall runoff	<input checked="" type="checkbox"/>	
Flood	<input checked="" type="checkbox"/>	
Tsunami/action of the sea	<input checked="" type="checkbox"/>	
Theft	<input checked="" type="checkbox"/>	Theft by persons living with you is excluded
Accidental glass breakage	PARTIAL	Maximum payment for each event is \$750
Sudden escape of liquid	<input checked="" type="checkbox"/>	Damage from liquid escaping slowly is excluded