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**Extending unfair contract terms protections to insurance contracts
Proposals Paper June 2018**

Thank you for the opportunity to provide this submission in response to the Proposals Paper Extending unfair contract terms protections to insurance contracts.

1. ABOUT NIBA AND INSURANCE BROKERS

- (a) NIBA is the industry association for insurance brokers across Australia. The association has around 350 member firms, employing over 4,000 insurance brokers in all States and Territories, in the cities, towns and regions of Australia.
- (b) NIBA is committed to high standards of professionalism in insurance broking in Australia. Insurance brokers work with their clients to assist them to:
 - (i) understand and manage their risks, including the risk of loss of or damage to property as a result of adverse weather or other climate related events;
 - (ii) obtain appropriate insurance cover for their risks and their property; and
 - (iii) pursue claims under their policies when an insured event occurs, in which case the insurance broker becomes the advocate for the client during the assessment and resolution of the claim.
- (c) In some cases, insurance brokers may provide services for insurers under agency arrangements.
- (d) NIBA is always supportive of fair and reasonable improvements in consumer protection, implemented in accordance with sound regulatory

practice. There must however be a proper cost benefit analysis to show that the benefits clearly outweigh any consumer or industry detriment.

2. EXECUTIVE SUMMARY

2.1 Generally

- (a) NIBA's primary comments in relation to the proposals paper relate to the lack of clarity of the proposals and the likely results of this.
- (b) NIBA believes that it remains unclear that the benefits of these proposals outweigh the costs and notes that the findings of the Royal Commission will need to be factored in as well.
- (c) It is clear to NIBA that further discussion is required between stakeholders in relation to the above to achieve a fair and clear result for all concerned.
- (d) NIBA summarises its key issues and responses below.

2.2 Where should the changes be included?

- (a) It seems simpler to build any changes into the Insurance Contracts Act and not the ASIC Act, as it limits the legislation a person (be it the insured or insurer or others) must consider.
- (b) NIBA understands that Treasury has not identified how the proposed changes would interact with other provisions of the Insurance Contracts Act whether within or outside the Act. Several concerns arise in this regard which we note in our response.

2.3 Scope of contracts affected

- (a) The proposed changes will catch many commercial insurance contracts that are not commonly considered consumer/small business related and which would not be caught by the retail client definition in the Corporations Act or the standard cover types of the Insurance Contracts Act.
- (b) Consideration should be given to whether some of these should be excluded after a proper cost benefit analysis.

2.4 "Main subject matter" carve out from unfair contracts

- (a) The proposals paper approach is to limit the main subject matter carve out in relation to insurance to "terms that describe what is being insured".
- (b) The proposed limitation is unclear in many respects which we explain in this response.
- (c) The proposed express limitation for insurance is not replicated in existing law and appears to put insurers in a worse position than the current legislation. Currently, the main subject matter is not defined for other businesses and is left for the courts to determine.

- (d) We are concerned that no clear justification for taking this inconsistent approach has been given or any evidence provided in support.
- (e) The above can:
 - (i) lead to unnecessary and costly disputes;
 - (ii) affect insurer's ability to obtain reinsurance or properly price risk; and
 - (iii) increase the costs of insurance for consumers.
- (f) NIBA notes that the EU qualifies the concept by carving out terms which "clearly define or circumscribe the insured risk and the insurer's liability shall not be subject to such assessment since these restrictions are taken into account in calculating the premium paid by the consumer."
- (g) The UK appears to adopt the position of having:
 - (i) blacklisted terms – those that are deemed unfair;
 - (ii) grey terms – those that are subject to assessment for fairness – examples are listed; and
 - (iii) terms not in the above category that 'specify the main subject matter or are an assessment of the appropriateness of the price payable under the contract by comparison with the goods, digital content or services supplied under it - these are not subject to the unfairness test if they are both transparent and prominent. The UK appears to adopt a similar position to the EU regarding the view on what is excluded as main subject matter.
- (h) In New Zealand they do not qualify or define what is carved out as the "main subject matter" BUT rely on insurance specific carve outs in the unfair term test provisions which is essentially equivalent to the EU main subject matter approach (and also goes further in some respects).

2.5 "Legitimate interests" qualifier carve out from what would be an unfair term

- (a) The consultation paper proposes to qualify the existing unfair term carve out for legitimate interests by only including in the carve out terms that BOTH:
 - (i) reasonably reflect the underwriting risk accepted by the insurer in relation to the contract; and
 - (ii) do not disproportionately or unreasonably disadvantage the insured.
- (b) The above concepts are very unclear and we explain why in the response below.
- (c) The proposed qualifications are not replicated in existing law and appear to put insurers in a worse position than the current legislation. Currently,

the legitimate interest test is not qualified for other businesses and is left for the courts to determine.

- (d) We are concerned that no clear justification for taking this inconsistent approach has been given or any evidence provided in support.
- (e) We note that the EU, UK and New Zealand do not adopt this approach.
- (f) New Zealand deems insurance specific terms to be reasonably necessary to protect the insurer's legitimate interest without qualification of the type proposed in the consultation paper.
- (g) The above can:
 - (i) lead to unnecessary and costly disputes;
 - (ii) affect insurer's ability to obtain reinsurance or properly price risk; and
 - (iii) increase the costs of insurance for consumers.
- (h) We set out our detailed response below.

2.6 Timing

- (a) NIBA understands that there is no expected timing for the release of the proposed legislation yet. NIBA notes that and consideration of the results of the Royal Commission will be important as well as the other Government proposals, such as the standard cover proposals, disclosure and standard definitions, which we understand are to be released soon.
- (b) NIBA does not believe that the transition timing proposals will be sufficient given the significant changes to systems and training that would be required by all stakeholders.

2.7 Remedies

- (a) Given the lack of clarity and issues arising regarding remedies that we discuss in our response below (especially where a provision can be fair or unfair depending on the circumstances), consideration should be given as to whether only ASIC should have the right to seek a remedy for any breach. A similar position seems to have been adopted in New Zealand.

3. LEGISLATIVE MODELS

3.1 Proposals summarised

- (a) **Make changes to existing unfair contract provisions in ASIC Act proposed –**

NIBA Comment - no guidance or discussion is provided on how this will work in the context of other insurance specific legislation where there is a conflict. We understand this has not been done.

NIBA believes that this is crucial in order to perform a proper cost benefit analysis of the proposals and determine appropriate carve outs.

If a term is open to challenge under UCT, the net effect is that many provision of the Insurance Contracts Act (IC Act) will be rendered ineffective, be of little use or result in unnecessary duplication or costly challenge.

By way of example:

- *It should be considered as to whether it is appropriate to make it clear that any provision in a policy that reflects an insurer's rights under section 28 of the IC Act arising from noncompliance with the duty of disclosure or misrepresentation provisions is to be unaffected. This could avoid any confusion, duplication, inconsistency or unnecessary challenges.*
- *The IC Act imposes certain minimum cover rules in section 34-35 which apply automatic minimum cover unless the insurer notifies the insured they won't be providing the minimum cover. The proposals should make it clear that where:*
 - *the minimum cover is provided as described; or*
 - *or more than minimum cover provided but the minimum cover exclusions are applies as applicable and this additional cover includes the minimum cover permitted exclusions,*

the minimum cover or minimum cover exclusions should not be subject to unfairness testing.

- *An insurer is exempt from mid-term variation provisions to the prejudice of the insured in the IC Act for certain specifically excluded types of policies i.e. section 53 won't apply in such cases. The UCT could create a result inconsistent with this and it may not be appropriate.*
- *Under section 54 an insurer may not refuse to pay claims in certain circumstances. Where the effect of a contract of insurance would, but for section 54, be that the insurer may refuse to pay a claim, either in whole or in part, by reason of some act of the insured or of some other person, being an act that occurred after the contract was entered into but not being an act in respect of which subsection (2) applies, the insurer may not refuse to pay the claim by reason only of that act but the insurer's liability in respect of the claim is reduced by the amount that fairly represents the extent to which the insurer's interests were prejudiced as a result of that act.*

Sub section (2) provides that subject to the succeeding provisions of this section, where the act could reasonably be regarded as being capable of causing or contributing to a loss in respect of which insurance cover is provided by the contract, the insurer may refuse to pay the claim.

The courts have found that section 54 will not apply in relation to “a restriction or limitation which must necessarily be acknowledged in the making of a claim, having regard to the type of insurance contract under which that claim is made.”

The UCT may mean that this approach will be open to challenge.

In cases where an insurer could rely on section 54(2) to refuse to pay a claim if for a provision of the type specified, is it the intent that such a provision can still be found invalid under UCT laws?

If so, section 54 becomes useless until the UCT issue is first tested.

- *The same result would appear to apply to the duty of utmost good faith provisions under section 13 and 14 to the extent the UCT provides greater remedies. Section 12 of the IC Act provides that the Part relating to the duty of utmost good faith cannot be read down. How is this expected to affect the UCT terms?*

A proper analysis is required and clear carve outs provided to avoid any confusion.

- *Consideration should be given to clarifying that anything insurers are permitted to do under the Act are terms that are “required or expressly permitted by law.”*

(b) Amend Insurance Contracts Act duty of Utmost Good faith to build in provisions

NIBA Comment - May be neater and may reduce compliance costs and complexity of two pieces of legislation. No proposals are provided on what would be required.

(c) Amend Insurance Contracts Act to have stand-alone UCT provisions

NIBA Comment - May be neater and may reduce compliance costs and complexity of two pieces of legislation. No proposals are provided on what would be required.

4. OBJECTIVES IN CONSULTATION PAPER

- (a) To ensure that consumers and small businesses who purchase insurance have the same access to protection from unfair terms in insurance contracts as they do for other contracts for financial products and services.

NIBA Comment - It will not be the same. The protection will be greater than for other industries creating an uneven playing field.

- (b) Increase incentives for insurers to improve the clarity and transparency of contract terms, and remove potentially unfair terms from their contracts.

NIBA Comment - It will do this but the changes as proposed appear to create significant uncertainty and could increase the pricing of risk. The proposals do not comment on the standard terms proposals that Government has proposed. Is the intent that Insurance Contracts Act standard minimum cover provisions be subject to attack? It is also not discussed how the changes would operate in the context of the Insurance Contracts Act as noted above.

- (c) Provide appropriate remedies for consumers and enforcement powers for the Australian Securities and Investments Commission (ASIC).

NIBA Comment - Significant remedies are provided to both. If there is a lack of clarity it may result in higher numbers of disputes and price increases to cover this risk.

- (d) The Consultation paper notes that extending the UCT laws to insurance contracts will also bring Australia into line with comparable jurisdictions, including the United Kingdom, the European Union and New Zealand, where insurance contracts are not excluded from those jurisdictions' UCT laws.

NIBA Comment - On NIBA's understanding of the other jurisdictions, the proposed regime is inconsistent with them in a significant manner as they all AT LEAST seem to exclude:

- *terms that identify the uncertain event;*
- *terms that otherwise specify the subject matter insured or the risk insured against; and*
- *terms that exclude or limit the liability of the insurer to indemnify the insured on the happening of certain events or on the existence of certain circumstances.*

5. MODEL OPTIONS

5.1 Proposed model

- (a) The key elements of the proposed model are:
- (i) Amending section 15 of the IC Act to allow the current UCT laws in the ASIC Act to apply to insurance contracts regulated by the IC Act.
 - (ii) The UCT provisions in the ASIC Act being tailored in their application to contracts of insurance to accommodate specific features of these contracts, in particular:
 - (A) the 'main subject matter' of an insurance contract will be defined narrowly as terms that describe what is being insured, for example, a house, a person or a motor vehicle;

- (B) clarification will be provided that the 'upfront price' will include the premium and the excess payable and that these will not be subject to review;
 - (C) a contract will be considered as standard form even if the consumer or small business can choose from various options of policy coverage;
 - (D) when determining whether a term is unfair, a term will be reasonably necessary to protect the legitimate interests of an insurer if it reasonably reflects the underwriting risk accepted by the insurer in relation to the contract and it does not disproportionately or unreasonably disadvantage the insured;
 - (E) examples specific to insurance will be added to the list of examples of kinds of terms that may be unfair which could include terms that permit the insurer to pay a claim based on the cost of repair or replacement that may be achieved by the insurer, but could not be reasonably achieved by the policyholder;
 - (F) where a term is found to be unfair, as an alternative to the term being declared void, a court will be able to make other orders if it deems that more appropriate;
 - (G) the definition of 'consumer contract' and 'small business contract' will include contracts that are expressed to be for the benefit of an individual or small business, but who are not a party to the contract;
 - (H) for life policies, as defined by the Life Insurance Act 1995, which are guaranteed renewable, it will be made clear that a term which provides a life insurer with the ability to unilaterally increase premiums will not be considered unfair in circumstances in which the premium increase is within the limits and under the circumstances specified in the policy.
- (b) The Consultation paper notes that the benefits of this proposed model include:
- (i) it will ensure that insureds are provided with protection under the same UCT laws which are already available to consumers in relation to other financial products and services. This will enable the courts, consumers, external dispute resolution schemes, and the regulator to take a consistent approach.

NIBA Comment - This creates a different regime and set of rules likely to create inconsistency.
 - (ii) it is consistent with the objective of the Australian Consumer Law that the UCT protections should be applied economy wide.

NIBA Comment - This creates a different regime and set of rules likely to create inconsistency and an uneven playing field

- (iii) it will not negatively affect or create uncertainty regarding the judicial interpretation of the IC Act and its existing legal principles and consumer protections.

NIBA Comment - At no point is there any discussion of how the IC Act and other legislation will operate in conjunction with this law, to the extent there may be an inconsistency.

5.2 Enhance existing IC Act remedies

- (a) Under this option, the existing remedies in the IC Act, particularly the duty of utmost good faith, would be enhanced to improve their effectiveness to provide UCT protections in relation to standard form insurance contracts.
- (b) Specifically, the possible changes could include the following elements:
 - (i) introduce a definition of an unfair term, with the definition reflecting the ASIC Act definition, with appropriate exemptions (for example, relating to the 'main subject matter' of the contract);
 - (ii) an unfair term will be a breach of the duty of utmost good faith and consistent with the existing remedy for this breach, an unfair term must not be relied on;
 - (iii) reversing the onus of proof, so where an insurer is relying on a term in the contract that a policyholder or third-party beneficiary considers is unfair, the insurer will be required to demonstrate that reliance on the term is not a breach of the duty of utmost good faith; and
 - (iv) enabling consumers or ASIC to seek court orders to remedy any disadvantage arising from an unfair term.
- (c) Section 15 of the IC Act would continue to operate so that the UCT provisions of the ASIC Act would not apply.

5.3 Introduce the existing UCT laws into the IC Act

- (a) Under this option, the IC Act would be amended to introduce a stand-alone set of UCT protections in the IC Act which largely mirror those in the ASIC Act, but with tailoring to take account of the specific features of insurance contracts and the existing regulatory framework of the IC Act.
- (b) Again, section 15 of the IC Act would continue to operate so that the unfair contract terms provisions of the ASIC Act would not apply.

5.4 Questions

- (a) **Do you support the proposal to amend section 15 of the IC Act to allow the current UCT laws in the ASIC Act to apply to insurance contracts regulated by the IC Act?**

NIBA Comment - NIBA is always supportive of fair and reasonable improvements in consumer protection, implemented in accordance with sound regulatory practice. There must however be a proper cost benefit analysis to show that the benefits clearly outweigh any consumer or industry detriment. We are not convinced this has been done to the extent required.

(b) What are the advantages and disadvantages of this proposal?

NIBA comment - We have listed these in this response. NIBA notes that it is incumbent on Government when making such a proposal to have considered such matters. The proposals paper appears to have gaps in this regard. For example, we understand that Treasury has not considered how the proposals would interact with the existing provisions of the Insurance Contracts Act and the proposals paper provides no useful information in this regard.

(c) What costs will be incurred by insurers to comply with the proposed model? To the extent possible, identify the magnitude of costs and a breakdown of categories (for example, substantive and/or administrative compliance costs in reviewing contracts).

NIBA comment - Based on current proposals and lack of clarity and limited transition period the costs are likely to be significant, especially in relation to insurance caught by UCT that is not subject to the Corporations Act retail client classes or standard cover provisions of the IC Act.

(d) Do you support either of the other options for extending UCT protections to insurance contracts?

NIBA comment - Enhancing existing IC Act remedies may be a simpler model subject to feedback below regarding main subject matter carve outs and other issues re the unfair contracts proposals. It could avoid any confusion as to applicable legislation and simplify training and the risk of any inconsistency of laws.

(e) What are the advantages and disadvantages of these options?

NIBA comment - As above.

(f) What costs would be incurred by insurers to comply with these options? To the extent possible please identify the magnitude of costs and a breakdown of categories (for example, substantive and/or administrative compliance costs).

NIBA comment – As above.

6. TYPES OF CONTRACTS CAUGHT

(a) *NIBA notes that the UCT legislation catches consumer and small business standard form contracts as defined in the Act.*

(b) *This means that it:*

- (i) *will apply to insurance contracts beyond those covered as retail client insurance products in the Corporations Act and the standard cover/prescribed products in the IC Act.*

This may or may not be appropriate in certain cases.

For example, a Corporate group purchases a professional indemnity policy covering all members, only one of which is a small business. The same Corporate group may purchase an ISR policy which also covers an individual director for a personal item of property. If the term is unfair only in the context of the individual small business or individual and is void this can have a significant impact on other participants.

Has any consideration been given to this issue or whether the protection in an insurance context should be limited in certain ways, especially in the context of group insurance arrangements? See comments on group policies further below.

- (ii) *may or may not apply to the same type of contract depending on whether the product is offered directly to a consumer or arranged via an intermediary acting in the consumer's interest.*

7. TERMS EXCLUDED FROM THE UCT LAWS

7.1 Generally

- (a) The UCT laws provide that the following terms are excluded from review:
 - (i) terms that define the main subject matter of the contract (the 'main subject matter' exclusion);
 - (ii) terms that set the upfront price payable under the contract; or
 - (iii) terms that are required or expressly permitted by law.

Section 12BI of the Australian Securities and Investments Commission Act 2001.

7.2 Main Subject Matter

- (a) Under the current UCT laws, the main subject matter of a contract is not defined in legislation and is a matter for the courts to decide on a case-by-case basis.
- (b) Because of this uncertainty, it is proposed that the main subject matter will be given a tailored definition for insurance contracts – Possible approaches:
 - (i) **Narrow definition (preferred approach)** - provide a narrow definition which excludes from review, terms that describe what is being insured, for example, a house, a person or a motor vehicle. A narrow definition would provide the most comprehensive scope for UCT protections. For example, policy limitations, conditions

precedent to cover and exclusions that affect the scope of cover would not be considered part of the 'main subject matter' and would be open to review.

For example, under a home and contents policy, terms excluded from review would include those which detail the insured property, such as the location and type of dwelling. The rationale for this proposal includes:

- (A) the objective of the UCT regime is to address the power imbalance that arises from contracts being offered to consumers on a take-it-or-leave-it basis. Therefore, the 'main subject matter' exclusion should be defined in a way that best serves this consumer protection objective;
- (B) it is consistent with the objective of the Australian Consumer Law that UCT protections should be given a broad application; and
- (C) it reduces the risk that UCT protections will be diminished by contractual drafting techniques or consumers being uncertain about which terms are subject to review.

The paper concludes that the proposed main subject matter exclusion only relates to defining which terms are open to review, it does not relate to whether or not the term is unfair. To determine this, the court will apply the test of unfairness. This approach seeks to strike an appropriate balance between the interests of both policyholders and insurers.

- (ii) **Broader definition** - provide a broader definition which would exempt from review terms that define the scope of cover. The approach adopted in the EU provides an example of such a definition via ECD - 93/13 which exempts from the UCT regime terms which 'clearly define or circumscribe the insured risk and the insurer's liability'.

7.3 Questions

- (a) ***Do you consider that a tailored 'main subject matter' exclusion is necessary?***

NIBA comment - In terms of what is proposed, the consultation paper notes that the concept will only cover terms that "describe what is being insured, for example, a house, a person or a motor vehicle".

It then gives as an example a home and contents policy, and notes that terms excluded from review would include "those which detail the insured property, such as the location and type of dwelling".

The concept of "describes what is being insured" and the example which appears to refer to the attribute of the dwelling ie "the type" create a lack of clarity.

For example, what is a “type of dwelling”, is it a house vs apartment etc and if so, does it extend to the materials of the building such as brick or timber, and if so, does it also extend to the “usage” of the dwelling e.g domestic or business usage and so on?

In terms of a person’s insured under an indemnity policy, how is the “description” concept to be interpreted?

Is it just the named person or also the role they are being covered for e.g as a director or officer or for business purposes only?

Where the line should be drawn is unclear.

Assuming the above can be clarified to the narrowest extent possible to exclude usage or roles etc this means any provisions dealing with the “scope of cover” are subject to challenge as an unfair term.

NIBA notes that this is inconsistent with the EU, UK and New Zealand positions.

The EU in Recital 19 of the EC Directive 93/13/EEC on Unfair Terms in Consumer Contracts provides [our bold italics]:

*“Whereas, for the purposes of this Directive, assessment of unfair character shall not be made of terms which describe the main subject matter of the contract nor the quality/price ratio of the goods or services supplied; whereas the main subject matter of the contract and the price/ratio may nevertheless be taken into account in assessing the fairness of terms; whereas it follows, inter alia, that in insurance contracts, **the terms which clearly define or circumscribe the insured risk and the insurer’s liability shall not be subject to such assessment since these restrictions are taken into account in calculating the premium paid by the consumer.**” (our emphasis)*

NIBA understands that the above generally has the result that the terms which clearly define the insured risk and the insurer’s liability are not subject to the fairness assessment since these restrictions are taken into account in calculating the premium paid by the consumer.

Contractual terms falling within the concept of ‘the main subject-matter of the contract’, within the meaning of Article 4(2) of Directive 93/13, must be understood as being those that lay down the essential obligations of the contract and, as such, characterise it (see judgments in Caja de Ahorros y Monte de Piedad de Madrid, C-484/08, EU:C:2010:309, paragraph 34, and Kásler et Káslerné Rábai, C-26/13, EU:C:2014:282, paragraph 49).

Terms ancillary to those that define the very essence of the contractual relationship cannot fall within the concept of ‘the main subject-matter of the contract’, within the meaning of that provision (judgments in Kásler et Káslerné Rábai, C-26/13, EU:C:2014:282, paragraph 50, and Matei, C-143/13, EU:C:2015:127, paragraph 54).

The UK appears to adopt the position of having:

- (i) *blacklisted terms – those that are deemed unfair;*
- (ii) *grey terms – If the term is not ‘blacklisted’ it may still be subject to assessment. The UK legislation provides examples of terms which may be unfair and thus subject to the fairness test. They are set out in a non-exhaustive list:*
 - (A) *terms that apply disproportionately high charges where the customer decides to cancel the contract;*
 - (B) *terms enabling the firm to determine the characteristics of the subject matter of the contract after the conclusion of the contract; and,*
 - (C) *terms allowing the trader to determine the price after the consumer is bound by the agreement.*
 - (D) *a term which has the object or effect of irrevocably binding the consumer to terms with which the consumer has had no real opportunity of becoming acquainted before the conclusion of the contract.*
 - (E) *a term which has the object or effect of allowing the trader to transfer the trader’s rights and obligations under the contract, where this may reduce the guarantees for the consumer, without the consumer’s agreement.*
- (iii) *terms not in the above category that ‘specify the main subject matter or are an assessment of the appropriateness of the price payable under the contract by comparison with the goods, digital content or services supplied under it - these are not subject to the unfairness test if they are both transparent and prominent. The UK appears to adopt a similar position to the EU regarding the view on what is excluded as main subject matter.*
- (b) *In New Zealand they do not qualify or define what is carved out as the “main subject matter”. Instead, they apply specific insurance carve outs in the provisions dealing with unfair terms by deeming the following terms to be terms that are reasonably necessary in order to protect the legitimate interests of the insurer (in effect removing them from the regime):*
 - (A) *a term that identifies the uncertain event or that otherwise specifies the subject matter insured or the risk insured against:*
 - (B) *a term that specifies the sum or sums insured or assured:*
 - (C) *a term that excludes or limits the liability of the insurer to indemnify the insured on the happening of certain events or on the existence of certain circumstances:*
 - (D) *a term that describes the basis on which claims may be settled or that specifies any contributory sum due from, or*

amount to be borne by, an insured in the event of a claim under the contract of insurance:

- (E) *a term that provides for the payment of the premium:*
- (F) *a term relating to the duty of utmost good faith that applies to parties to a contract of insurance:*
- (G) *a term specifying requirements for disclosure or relating to the effect of non-disclosure or misrepresentation, by the insured.*

If yes, do you support this proposal or should an alternative definition be considered?

NIBA comment - Further discussion is required between stakeholders in relation to the above to achieve a fair and clear result for all concerned.

- (c) ***Should tailoring specific to either general or life insurance contracts also be considered?***

NIBA comment – This is likely to be sensible. Further discussion is required between stakeholders in relation to the above to achieve a fair and clear result for all concerned.

8. Upfront Price

- (a) The UCT laws provide that terms setting the contract's upfront price are excluded from review. It is proposed that for insurance contracts:
 - (i) the upfront price will include the premium paid, or to be paid, by the insured and therefore excluded from review.
 - (ii) the quantum of the excess payable under an insurance contract should be considered part of the upfront price and, therefore, excluded from review.

8.2 Questions

- (a) ***Do you support this proposal or should an alternative proposal be considered?***

NIBA comment - NIBA supports this proposal and does not believe an alternative proposal should be considered. The exclusion of upfront prices is in all relevant legislation worldwide.

- (b) ***Do you agree that the quantum of the excess payable under an insurance contract should be considered part of the upfront price and, therefore, excluded from review?***

NIBA comment - As above.

- (c) ***Should additional tailoring specific to either general or life insurance contracts also be considered?***

NIBA comment – This is likely to be sensible. Further discussion is required between stakeholders in relation to the above to achieve a fair and clear result for all concerned.

9. STANDARD FORM CONTRACTS

9.1 Generally

- (a) In determining whether a contract is a standard form contract, a court may take into account such matters as it thinks relevant, but must take into account a number of factors, including whether:
- (i) one of the parties has all or most of the bargaining power relating to the transaction;
 - (ii) another party was, in effect, required either to accept or reject the terms of the contract in the form in which they were presented; and
 - (iii) the terms of the contract take into account the specific characteristics of another party or the particular transaction.
- (b) It is proposed that, for insurance contracts, a contract can be considered as standard form even if the consumer or small business can choose from various options of policy coverage (including, but not limited to, excess amounts, riders, sum insured amounts, and policy exclusions).

9.2 Questions

- (a) ***Is it necessary to clarify that insurance contracts that allow a consumer or small business to select from different policy options should still be considered standard form?***

NIBA comment – This may be sensible. Further discussion is required between stakeholders in relation to the above to achieve a fair and clear result for all concerned.

- (b) ***If yes, do you support this proposal or should an alternative definition be considered?***

NIBA comment – We would need to see the actual definition. Will the definition work in conjunction with the other factors or as an automatic carve out?

The risk is that the definition is drafted in a way that would catch a contract that should not otherwise be caught. We expect similar issues could arise for other contracts. Have any issues been identified? Further discussion is required between stakeholders in relation to the above to achieve a fair and clear result for all concerned.

10. MEANING OF UNFAIR

10.1 Generally

- (a) Under the UCT laws a term will be unfair if:
- (i) it would cause a significant imbalance in the parties' rights and obligations arising under the contract;
 - (ii) it is not reasonably necessary in order to protect the legitimate interests of the party who would be advantaged by the term; **and**
 - (iii) it would cause detriment (whether financial or otherwise) to a party if it were to be applied or relied on.
- (b) If one of the above tests is not met the term won't be considered unfair.
- (c) In determining whether a term is unfair, a court may take into account such matters as it thinks relevant, but must take into account:
- (i) the extent to which the term is transparent (that is, expressed in reasonably clear language, legible, presented clearly and readily available to any party affected by the term); and
 - (ii) the contract as a whole.
- (See Section 12BG and section 12BH of ASIC Act).
- (d) To provide guidance to insurers and consumers, the Consultation paper proposes to provide clarity about when a term is reasonably necessary to protect the legitimate interests of a party who would be advantaged by the term.
- (e) The proposed options are:
- (i) deem a term reasonably necessary to protect the insurer's legitimate interests when the insurer proves the term reasonably reflects the underwriting risk accepted by them in relation to the contract.

According to the consultation paper, this approach would provide that terms defining the insured risk and are taken into account in the calculation of the premium should not be considered unfair.

- (ii) deems a term reasonably necessary to protect the insurer's legitimate interests when the term reasonably reflects the underwriting risk accepted by the insurer in relation to the contract **and** it does not disproportionately or unreasonably disadvantage the insured. (The preferred approach).

The Consultation paper states that this is to allow a court to consider factors beyond whether a term is taken into account in the calculation of the premium.

For example, a term may only incidentally relate to the insurer's risk, or may have a relatively minor effect on an insurer's premium rating structure, but have a disproportionate effect on the policyholder.

The rationale for this includes:

- (A) it encourages appropriate risk bearing between insurers and consumers by incentivising insurers to ensure their contract terms accurately and transparently reflect their underwriting risk; and
- (B) it is consistent with the objective of the Australian Consumer Law that UCT laws should be given a broad application by reducing the risk for an insurer changing their premium rating structures to exclude terms from reviewability.

10.2 Questions

- (a) ***Do you consider that it is necessary to tailor the definition of unfairness in relation to insurance contracts?***

NIBA comment – This may be sensible. Further discussion is required between stakeholders in relation to the above to achieve a fair and clear result for all concerned.

- (b) ***Do you support the above proposal or should an alternative proposal be considered? For example, should the approach taken in New Zealand's Fair Trading Act be considered?***

NIBA comment - In relation to the proposal as described in the consultation paper, we make the following comments.

What is described in the consultation paper as “reasonably reflects the underwriting risk accepted by the insurer in relation to the contract” is unclear? No useful guidance is provided nor any examples.

The only explanation regarding this concept is “This approach would provide that terms defining the insured risk and are taken into account in the calculation of the premium should not be considered unfair.”

This explanation does not reflect the extremely broad words used to describe the concept “reasonably reflects the underwriting risk accepted by the insurer in relation to the contract”.

Such a concept imposes a reasonableness test on the provision. For example, on a plain reading a person could argue that even if a term defines the underwriting risk and is taken into account in the calculation of the premium (ie per the Consultation paper explanation), it could still be considered unfair if as a provision or as priced, it doesn't “reasonably reflect the underwriting risk actually accepted”.

If there is no clarity on where the line is to be drawn, regulators and consumers could consistently test the underwriting decisions of insurers at great expense to industry (and ultimately consumers) and expose the decision-making process to competitors with flow on competition law issues.

Is the test to be subjective or objective in terms of the insurer's position?

The additional factor, that it also not "disproportionately or unreasonably disadvantage the insured" is also unclear. In particular:

- (A) *is it to be the particular insured based on their subjective or objective personal circumstances or all insureds from a general perspective?*

If it is the individual insured, if the effect is to have the insurer cover a risk such as flood for one (or more insureds in equivalent circumstances) that according to the insurer ought not to be covered automatically, this would lead to an increase of premiums for the whole risk group in question – this can affect the social character of insurance;

- (B) *what is the relevant proportion of disadvantage that is sufficient to create an issue – there is no certainty on where the line can be drawn?*
- (C) *is the unreasonableness of the disadvantage a subjective or objective test in the context of the insurer's decision making?*

The above appears to make it difficult for an insurer to safely price its insurance and for reinsurers to do the same.

Has APRA, as regulatory of insurer solvency, been consulted on this?

The UK, EU and New Zealand have not adopted a similar approach.

Given the consequences of a breach, this level of ambiguity and its impact on the certainty of pricing, is concerning.

If there is a high volume of regulator or consumer testing of the underwriting decisions of insurers this could have a cost impact on industry (and ultimately consumers) and possibly expose decision-making processes to competitors with flow on competition law issues.

Further discussion is required between stakeholders in relation to the above to achieve a fair and clear result for all concerned.

- (c) **Should tailoring specific to either general or life insurance contracts also be considered?**

NIBA comment – This may be sensible. Further discussion is required between stakeholders in relation to the above to achieve a fair and clear result for all concerned.

11. TERMS THAT MAY BE CONSIDERED UNFAIR

11.1 Generally

- (a) The UCT laws provide a non-exhaustive list of examples of kinds of terms that may be unfair (Section 12BH of the Australian Securities and Investments Commission Act 2001). These examples provide guidance, but do not prohibit the use of these terms or create a legal presumption that they are unfair.
- (b) It is proposed that examples specific to insurance contracts will be added to this list. For example, the following kinds of terms could be added:
 - (i) terms that permit the insurer to pay a claim based on the cost of repair or replacement that may be achieved by the insurer, but could not be reasonably achieved by the policyholder;
 - (ii) terms which make the insured's ability to make a claim conditional on the conduct of a third-party over which the insured has no control; and
 - (iii) terms in a contract that is linked to another contract (for example, a credit contract) which limit the insured's ability to obtain a premium rebate on cancellation of the linked contract.

11.2 Questions

- (a) **Do you consider that it is necessary to add specific examples of potentially unfair terms in insurance contracts?**

NIBA comment – This may be sensible. Further discussion is required between stakeholders in relation to the above to achieve a fair and clear result for all concerned. The UK has some examples in an insurance context it uses in its grey list.

- (b) **Do you support the kinds of terms described in the proposal or should other examples be considered?**

NIBA comment – No information is provided on why these are considered unfair terms, nor scenarios of when and why this has been found to be the case. This should be done.

In many cases they will not be unfair and other cases unfair.

For example, the scenario where an insurer wishes to repair under the policy and has a right to do so, but the insured does not want this and wants a cash settlement. It would not seem unfair that the insurer rely on a term in such a case that permits it to pay a claim based on the cost of repair or replacement that may be achieved by the insurer, but could not be reasonably achieved by the policyholder, where it has priced the policy on this basis.

- (c) **Should tailoring specific to either general or life insurance contracts also be considered?**

NIBA comment - This may be sensible. Further discussion is required between stakeholders in relation to the above to achieve a fair and clear result for all concerned.

12. REMEDIES FOR UNFAIR TERMS

12.1 Generally

- (a) The UCT laws provide that if a term is declared unfair, it is void. This approach is consistent with other UCT laws internationally and ensures a counterbalancing in the rights of the parties.
- (b) In relation to what UCT remedy should apply to unfair terms in insurance contracts, options include:
- (i) the existing remedy of 'voidance'; or
 - (ii) that the insurer cannot rely on the term.
- (c) It is proposed that, consistent with the current UCT regime, the consequence of a term being found to be unfair will be that the term will be void. This will have consequences that include:
- (i) a declaration that a term is unfair will apply to contracts and parties on a case-by-case basis, acknowledging, however, that as the declaration will apply to a standard form contract, there is the potential that it could be considered unfair for a number of other consumers and small businesses;
 - (ii) ASIC may seek court orders to prevent or redress any disadvantage to a class of consumers or small businesses who are not a party to the contract but are impacted by the unfair term; and
 - (iii) an insurer that attempts to enforce or rely on an unfair term may be contravening the prohibitions against unconscionable and/or misleading or deceptive conduct under the ASIC Act. If this is the case, ASIC will be able to seek other orders in relation to the unfair term, including an injunction, compensation or declarations covering a class of consumers not party to the proceeding, but at risk of being disadvantaged by the unfair term.
- (d) A declaration that a term was unfair would not automatically lead to a conclusion that the insurer had breached provisions of the ASIC Act or had breached its duty of utmost good faith. However, courts would be free to draw those conclusions if the circumstances of the case compelled them to.
- (e) For insurance contracts, there may be circumstances where the remedy of voiding a term may not be the preferred outcome for a policyholder. For example, a particular term may unfairly limit the amount paid to a

policyholder under a claim, but to have the term made void may remove the basis for the claim entirely.

- (f) Therefore, as an alternative to the term being void, it is proposed that a court should also be able to make other orders if it thinks the order will provide a more appropriate and just outcome in all of the circumstances.

12.2 Questions

- (a) **Do you support the remedy for an unfair term being that the term will be void? Is a different remedy more appropriate (for example, that the term cannot be relied on)?**

NIBA comment – this may not always be appropriate – An insurance term can, depending on the circumstances, be fair or unfair in its application. See repair or replacement term above. Voiding it in fair application would not appear to be an appropriate remedy.

We note that in New Zealand, only the regulator ASIC, and not consumers, are permitted to apply for a declaration that a term is unfair.

Further discussion is required between stakeholders in relation to the above to achieve a fair and clear result for all concerned.

- (b) **Do you consider it is appropriate for a court to be able to make other orders?**

NIBA comment - Yes, but further discussion is required between stakeholders in relation to the above to achieve a fair and clear result for all concerned.

- (c) **Should tailoring specific to either general or life insurance contracts also be considered?**

NIBA comment - This may be sensible. Further discussion is required between stakeholders in relation to the above to achieve a fair and clear result for all concerned.

13. GROUP POLICIES AND THIRD-PARTY BENEFICIARIES

13.1 Generally

- (a) The UCT laws apply to certain 'consumer contracts' and 'small business contracts'. These definitions require a consumer or small business to be a party to the contract in order to be covered by UCT protections. For standard form contracts used throughout the economy, it will usually be the case that a person affected by an unfair term is a party to the contract.
- (b) Certain types of insurance policies extend benefits to third-party beneficiaries (either individually or as part of a class) who are not parties to the contract. For such contracts, it will be the third-party beneficiary, rather than the party to the contract that may potentially be affected by an unfair term. Examples of this include:

- (i) life insurance policies providing benefits to nominated beneficiaries. These can be entered into either directly by a consumer or by an entity such as a superannuation fund or employer under a group life policy; and
 - (ii) insurance taken out by a group purchasing body, such as a sporting association covering members of their club.
- (c) It is proposed that the UCT laws will apply to consumers and small businesses who are third-party beneficiaries under the contract. Specifically:
- (i) the definitions of 'consumer contracts' and 'small business contracts' will include contracts that are expressed to be for the benefit of an individual or small business but who are not a party to the contract; and
 - (ii) third-party beneficiaries would be able seek declarations that a term of a contract is unfair.
- (d) The rationale for this approach is that access to UCT protections by consumers and small businesses should be based on the actual risk or incidence of unfairness in contractual terms and not affected by how the insurance arrangements entered into for their benefit are structured or the nature of the group or master policyholder.

13.2 Questions

- (a) **Do you consider that UCT protections should apply to third-party beneficiaries?**

NIBA comment - It reasonable to apply appropriate protection to such persons to the extent they are directly affected.

It is unclear how the tests referred to above ie “reasonably reflects the underwriting risk and not “disproportionately or unreasonably disadvantage the insured” would be applied in a group context and also in circumstances where they pay nothing.

How are the actions of the group purchasing body to be taken into account?

Will this legislation potentially expose them to liability and create a disincentive for such schemes and the benefits they bring?

Further discussion is required between stakeholders in relation to the above to achieve a fair and clear result for all concerned.

- (b) **Do you support the above proposal or should an alternative proposal be considered?**

NIBA comment - Further discussion is required between stakeholders in relation to the above to achieve a fair and clear result for all concerned.

- (c) **Superannuation fund trustees may have substantial negotiating power and owe statutory and common law obligations to act in the best interest of fund members. Do these market and regulatory factors already provide protections comparable to UCT protections such that it would not be necessary to apply the UCT regime to such products?**

NIBA comment – NIBA has not conducted a comparison but it needs to be done for a view to be formed. Unfair playing field issues could arise. Further discussion is required between stakeholders in relation to the above to achieve a fair and clear result for all concerned.

14. TAILORING FOR SPECIFIC INSURANCE CONTRACTS

14.1 Generally

- (a) It is proposed that for life insurance contracts, it will be made clear that where a term provides a life insurer with the ability to unilaterally increase premiums, this will be considered to be fair where the premium increase is related to the management of the insurer's risk

Questions

- (b) **Do you consider that any other tailoring of the UCT laws is necessary to take into account specific features of general and/or life insurance contracts?**

NIBA comment - Further discussion is required between stakeholders in relation to the above to achieve a fair and clear result for all concerned. We expect carve outs and clarification will be required if the proposals are progressed due to the current ambiguity.

- (c) **Do you agree that unilateral premium adjustments by life insurers should not be considered unfair in circumstances in which the premium increase is within the limits and under the circumstances specified in the policy?**

NIBA Comment – Yes.

15. TRANSITIONAL ARRANGEMENTS

15.1 Generally

- (a) A 12 month transitional period will be provided before the new provisions take effect. After the transition, it is proposed that the UCT provisions will apply as follows:
- (i) New contracts: New provisions will apply to all new contracts originally entered into on or after the commencement.
 - (ii) Renewed contracts: If a contract that was originally entered into before the commencement is renewed, the new provisions will apply to the contract as renewed, on or after the day on which the renewal takes effect.

- (iii) Contract variations: If a contract was originally entered into before the commencement is varied on or after the day, the new provisions apply to the term as varied, on or after the day the variation takes effect. Other terms of that contract will not be made subject to the UCT provisions because of the variation, until such time as the contract is renewed.

Questions

- (b) **Is a 12 month transition period adequate? If not, what transition period would be appropriate?**

NIBA comment – We do not believe this is likely to be adequate. Product design and underwriting will need to be significantly reviewed, reinsurance arrangements renegotiated, and systems changes made which will take significant time and cost to implement, as will training.

Further discussion is required between stakeholders in relation to the above to achieve a fair and clear result for all concerned.

- (c) **Are the transition arrangements outlined above appropriate or should alternative transition arrangements be considered?**

NIBA comment - In New Zealand, the UCT provisions do not apply to variations of the terms of pre-existing insurance contracts or to new insurance contracts that effectively renew pre-existing contracts. See Section 26A(3) Fair Trading Act 1986 NZ.

Further discussion is required between stakeholders in relation to the above to achieve a fair and clear result for all concerned.

- (d) **What will insurers need to do during the transition period to be ready to comply with the new UCT laws?**

NIBA comment - Significant steps will be required, including:

- *Policy design review;*
- *Policy and associated documentation content review;*
- *Pricing review;*
- *Reinsurance review; and*
- *Distribution procedures review;*
- *Changes and training implemented regarding the above to affected systems and procedures.*

- (e) **Should tailoring specific to either general and/or life insurance contracts be considered?**

NIBA comment - Further discussion is required between stakeholders in relation to the above to achieve a fair and clear result for all concerned.

If you have any questions in relation to this submission, please do not hesitate to contact me.

Yours sincerely,

Dallas Booth
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