7 March 2019

Manager
Insurance and Financial Services Unit
The Treasury
Langton Crescent
PARKES ACT 2600

Dear manager

By email: InsuranceDisclosure@treasury.gov.au

Disclosure in general insurance: Improving consumer understanding

Discussion paper released in January

A submission by the Australian Financial Complaints Authority, providing feedback on the discussion paper, is attached. Thank you for granting an extension for the submission.

If we can assist by discussing issues, or providing further information, please do not hesitate to contact us. Our contact for this matter is our Policy & Liaison Adviser, Carolyn Bruns at cbruns@afca.org.au or on (03) 9613 7389.

Yours faithfully

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Australian Financial Complaints Authority Limited
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General insurance disclosure

Treasury discussion paper released in January 2019

AFCA submission

March 2019

Australian Financial Complaints Authority

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Introduction

The Australian Financial Complaints Authority (AFCA) is the new independent external dispute resolution (EDR) scheme for the financial sector. It replaces the Financial Ombudsman Service (FOS), the Credit and Investments Ombudsman (CIO) and the Superannuation Complaints Tribunal (SCT).[1]

AFCA's purpose is to provide fair, independent and effective solutions for financial disputes. It does this not only by providing fair dispute resolution services, but also by working with financial firms to improve their processes and drive up industry standards of service, thereby minimising disputes.

More broadly, AFCA will play a key role in restoring trust in the financial services sector.

In addition to providing fair, independent and effective solutions for financial disputes, AFCA has responsibilities[2] to identify, resolve and report on systemic issues and to notify the Australian Securities and Investments Commission (ASIC) of serious contraventions of the law, which go beyond individual complaint resolution.

On 1 May 2018, AFCA was authorised pursuant to the *Corporations Act 2001.* The AFCA Rules, which govern our operations, were approved by ASIC in September 2018. We began to receive complaints under these rules on 1 November 2018.

AFCA welcomes the opportunity to provide feedback on the discussion paper *Disclosure in general insurance: Improving consumer understanding* released by Treasury in January 2019 (Discussion Paper). This submission[3] draws on the experience of the predecessors of AFCA – organisations that have handled general insurance complaints for more than 25 years.

Key points in this submission are:

Premium increases and component pricing

AFCA believes that renewal notices should be required to disclose:

- component pricing, including information on items such as flood cover and taxes
- the previous year's premium, sum insured and excess, and possibly taxes for the that year
- an explanation of any premium increase.

[1] The Appendix provides a brief overview of AFCA. For comprehensive information about AFCA, see our website www.afca.org.au.
[2] See ASIC's Regulatory Guide 267 *Oversight of the Australian Financial Complaints Authority.*
[3] This submission has been prepared by the staff of AFCA and does not necessarily represent the views of individual directors of AFCA.

Providing this disclosure at the renewal stage would significantly help consumers to raise informed questions and, if necessary, seek alternative insurance.

We also strongly support the approach of requiring new quotes and renewal notices to include a link to ASIC's MoneySmart website.

Standard cover regime

The standard cover regime is valuable, as it discourages the development of low value products as well as helping consumers to compare products. However, the regime needs to be improved. Recent statistics show that policy holders do not understand their policies well and there is reason to believe the statistics do not reflect the full extent of this problem.

AFCA believes that enhancements to the standard cover regime should be made along the lines recommended in an interim report released recently by the Australian Consumer and Competition Commission (ACCC). We believe consideration should also be given to:

- basing standard cover on **minimum coverage** designed to have low premiums and allowing insurers to add extra features (for higher premiums disclosed clearly)
- requiring a participating insurer to provide minimum coverage at **three levels** – basic, intermediate and premium (and allowing extra features to be added to insurance at any level).

Standard definitions

AFCA considers that standardisation of the definition of 'flood' has reduced dispute levels and consumer confusion. In our view, definitions of other key terms – including 'action of the sea', 'impacts' and 'storm' - should be standardised.

Key facts sheets

AFCA recommends that enhancements to key facts sheet (KFS) requirements be coordinated with reforms to the standard cover regime and the standardisation of definitions. In our assessment, KFSs are most likely to improve disclosure for insurance policies within this regime that use terms with standardised definitions.

We consider it is crucial to:

- keep KFSs short and clear
- design KFSs to be used with – not instead of – product disclosure statements.

Innovative disclosure

Technology now enables insurers to obtain precise information about an individual property to use when pricing the risk of insuring the property.

Requiring insurers to disclose this information to the property owners in the processes of quoting for new insurance and renewals could increase transparency. It could also give these consumers more information to draw on when making insurance decisions or considering risk mitigation to reduce premiums.

1. Premium increases and component pricing

AFCA strongly supports the core proposals for disclosure through renewal notices examined in the Discussion Paper, which would require a notice to disclose:

- component pricing
- the previous year's premium
- an explanation of any premium increase.

Providing this disclosure at the renewal stage would help consumers to raise informed questions and, if necessary, seek alternative insurance.

In component pricing disclosure, we consider that information about pricing of flood cover would be particularly helpful. Taxes are another component that should be disclosed to inform consumers properly.

As acknowledged in the Discussion Paper, consumers need to consider factors other than premiums when renewing insurance. We believe that renewal notices should disclose not only the previous year's premium but also the sum insured and excess for that year. In our view, information about excesses is very useful for consumers and enables them to make informed decisions about cover. Flexible excesses can make insurance more affordable. To enable consumers to compare renewal arrangements with existing insurance, a renewal notice could also disclose the tax component of pricing for the previous year.

In its interim report on a current inquiry, ACCC recommended that new quotes and renewal notices should be required to include a link to ASIC's MoneySmart website[4]. AFCA agrees that this requirement should be imposed, to help consumers make decisions about insurance purchases and renewals. We note the ACCC's recommendation was made in a review of home insurance. It may be appropriate to impose the same requirement for all general insurance products.

2. Standard cover regime

The standard cover regime was established to standardise terms and conditions of cover for certain types of insurance. Although this standardisation has not occurred, AFCA considers that the regime should be improved by modification rather than replaced. The regime is important not only to make it easier for consumers to compare products but also to discourage the development of low value products, which present a particular risk to people with poor financial literacy who are unlikely to understand the products' deficiencies.

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[4] Recommendation 7 in *Northern Australia Insurance Inquiry: First Interim Report* released by ACCC in November 2018.

2.1 Statistics

Claims statistics in the report *General Insurance in Australia 2016-17* released by the General Insurance Code Governance Committee in March 2018 (Code Report) indicate that the standard cover regime is not working well. Key retail general insurance figures for the year 2016-17[5] are as follows:

Claims lodged	4,022,089
Claims declined	158,546
Claims withdrawn[6]	279,698

The Code Report states the acceptance rate for retail claims for 2016-17 was 95.8%. This was calculated by:

- using an adjusted figure for claims lodged (X) which excludes claims withdrawn
- expressing X less claims declined as a percentage of X[7].

The Code Report explains that claims data does not provide a complete, accurate indication of claims activity.[8] For example, claims were recorded as accepted even if they were partly accepted (and partly declined). The result is that the 95.8% acceptance rate statistic involves an element of claim denial. We understand that, from year to year, a significant number of claims are partly declined.

The claims figures in the table above show that, of about 4 million claims on retail insurance lodged, 438,244 - over 10% - were declined completely or withdrawn.

AFCA is concerned that this rate of over 10% indicates policy holders do not have a good understanding of their policies. This problem is likely to be greater than the figures above suggest given that claims declined statistics do not reflect claims partly declined.

2.2 Suggestions

As the Discussion Paper explains, for the standard cover regime to facilitate product comparison more effectively, key terms used in policies need to be defined consistently. The current ACCC inquiry also identifies factors that could be addressed to improve the standard cover regime. Examples include:

- The regime does not make it mandatory for a participating insurer to provide a product fully consistent with standard cover. Making this mandatory would give consumers a reference point to use when comparing different products.
- The regime does not set minimum standards for insurance.

[5] Page 20 of Code Report.
[6] Includes withdrawals by insurers as well as claimants.
[7] Page 27 of Code Report
[8] Page 20 of Code Report.

- Insurers providing products that depart from standard cover are not required to make the departures clear or explain how they affect premiums.
- Features included in standard cover do not accord with the features most commonly included in products at present.
- The regime only applies to some types of insurance. For example, it does not apply to building insurance for strata title residences.

On page 146 of its interim report, the ACCC describes an alternative approach and AFCA supports moving to an approach along those lines. However, we believe that consideration should also be given to:

- basing standard cover on **minimum coverage** designed to have low premiums and allowing insurers to add extra features (for higher premiums disclosed clearly)
- requiring a participating insurer to provide minimum coverage at **three levels** – basic, intermediate and premium (and allowing extra features to be added to insurance at any level).

Arrangements are in place at present enabling people with special needs, such as remote communities, to obtain basic, inexpensive insurance for essential items including household appliances and vehicles. When the standard cover regime is reviewed, care should be taken to ensure changes do not disrupt these existing arrangements. It may be necessary to enable these arrangements to continue – perhaps where they have ASIC approval or meet specified requirements – as an exception to the general regime.

3. Standard definitions

It has already been accepted that standard definitions of key terms should be developed and implemented. Standardisation of definitions is particularly important for the standard cover regime.

AFCA strongly agrees with Recommendation 4 in the ACCC's interim report, which is to standardise the definitions of prescribed events including 'action of the sea', 'impacts' and 'storm'. We consider that definitions of other terms should also be standardised. By consulting with industry and consumer groups, it should be possible to identify areas where inconsistent definitions create problems.

Our view is that the standardisation of the definition of 'flood' has benefitted consumers and industry by reducing dispute levels and consumer confusion. The table below provides information relating to two natural disasters – the Brisbane floods that occurred before the flood definition was standardised and Cyclone Debbie, which occurred after the standardisation was implemented. For Cyclone Debbie, estimated insured losses were higher and more insurance claims were lodged, but far fewer disputes reached EDR.

	Brisbane floods January 2011	Cyclone Debbie March - April 2017
Insured loss[9]	$1,356m	$1,775m
Claims lodged	58,463[10]	73,258[11]
Disputes received by AFCA/FOS	1301	374

4. Key facts sheets

The starting point for AFCA's comments on KFS requirements is that consumers considering an insurance product need to understand its product disclosure statement. KFSs should be designed to be used with – not instead of – product disclosure statements. To help consumers, KFSs should be kept short and clear.

Extending the use of KFSs to a wider range of general insurance may be worthwhile. AFCA recommends that enhancements to KFS requirements be coordinated with reforms to the standard cover regime. In our assessment, KFSs are most likely to improve disclosure for insurance policies within the standard cover regime that use terms with standardised definitions. If products are truly comparable, brief documents highlighting key features are likely to be effective. Brief documents could not be expected to explain or even identify complicated details of products.

The Discussion Paper refers to research indicating that consumer awareness of KFSs is low and invites suggestions to address this issue. If regulatory requirements are revised to ensure KFSs operate effectively, as part of the standard cover regime, KFSs should in our view be made more prominent in product information provided online.

5. Innovative disclosure

Technology now enables insurers to obtain precise information about an individual property to use when pricing the risk of insuring the property. For example, an insurer can obtain photographs to show where a residence is located on land, its exterior and whether it is elevated from the ground.

[9] Source: estimate by Insurance Council of Australia (ICA) as at 2017 in ICA Catastrophe Dataset linked to page 22 of Code Report.

[10] Source: estimate by ICA referred to on page 289 of *Queensland Floods Commission of Inquiry Final Report* released in March 2012.

[11] Source: Page 22 of Code Report.

Requiring insurers to disclose this type of information to the property owners in the processes of quoting for new insurance and renewals could increase transparency. It could also give these consumers more information to draw on when making insurance decisions or considering risk mitigation to reduce premiums.

Appendix – About AFCA

AFCA is a free, fair and independent dispute resolution scheme. AFCA's service is offered as an alternative to tribunals and courts to resolve complaints that individual and small business consumers have with their financial firms. We consider complaints about:

- credit, finance and loans
- insurance
- banking deposits and payments
- investments and financial advice
- superannuation.

AFCA's role is to assist consumers to reach agreements with financial firms about how to resolve their complaints. We are impartial and independent. We do not act for either party to advocate their position. If a complaint does not resolve between the parties, we will decide an appropriate outcome.

Decisions made by AFCA can be binding on the financial firm involved in a complaint. We can award compensation for losses suffered because of a financial firm's error or inappropriate conduct. There are other remedies we can also provide for superannuation complaints.

AFCA is not a government department or agency, and is not a regulator of the financial services industry. We are a not-for-profit company, limited by guarantee, governed by a board with equal numbers of industry and consumer representatives. AFCA's Chief Ombudsman is responsible for the management of the organisation.

Under transitional arrangements that have been put in place with ASIC's approval, AFCA is currently resolving complaints made to FOS and CIO and will continue to do so until they are resolved. These complaints will be handled in accordance with the FOS Terms of Reference or CIO Rules, as applicable and in force when the relevant complaint was lodged.

AFCA is built upon the work of FOS, CIO and SCT.[12] However, in time, AFCA will develop new approaches informed, but not bound, by those predecessor schemes' approaches to resolving disputes.

[12] A joint working group headed by Dr Malcom Edey was established and the schemes collaborated to develop AFCA and integrate the superannuation jurisdiction.