



ASIC
Australian Securities &
Investments Commission

Disclosure in general insurance: Improving consumer understanding

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Executive summary

- 1 The Australian Securities and Investments Commission (ASIC) welcomes the opportunity to provide comments on proposals raised in Treasury’s discussion paper, [*Disclosure in general insurance: Improving consumer understanding*](#) of January 2019.
- 2 The strength of the evidence about the limitations of disclosure indicates that it is important to move beyond a presumption that disclosure is always the right, default, or only, regulatory tool to address issues of concern in the general insurance market. Disclosure will continue to have a role, but it is important that its effectiveness not be over-stated and that it is complemented by the development and employment of more effective regulatory tools.
- 3 The insights and recommendations of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services provide an opportunity to refocus from an over-reliance on disclosure to fix problems resulting from misaligned incentives and poorly designed products.
- 4 In particular, the proposed product design and distribution obligations will provide increased accountability for issuers and distributors across the product life cycle, rebalancing the responsibility for product suitability decisions between consumers and industry. Together with the proposed product intervention power, these reforms will allow ASIC to take a broader regulatory approach beyond disclosure-based interventions to improve consumer outcomes.
- 5 To maximise the opportunity afforded by these new powers, ASIC considers it important that they be prioritised in the Government’s reform agenda, along with the proposed application to insurance contracts of the unfair contract provisions in the *Australian Securities and Investments Commission Act 2001*.
- 6 The Financial System Inquiry (FSI) gave the general insurance industry the task of reducing complexity and improving consumer understanding. Progress made since this issue was flagged in 2014 has been modest. The question for the insurance industry becomes how it can move beyond ‘innovative disclosure’ initiatives, and take an integrated approach to product design, sales and marketing processes to improve the understanding and outcomes of its customers.
- 7 As an initial step for improved product design, ASIC considers that insurers should offer products that provide standard cover. This could be done while insurers continue to offer existing products that diverge from standard cover. Such an approach would enable consumers to access the benefits of the standard cover regime and provide them with greater certainty.

- 8 Notwithstanding the limitations of disclosure, ASIC supports disclosing the previous year's premium on renewal notices. This would encourage competition and comparability and allow transparent price comparisons.
- 9 ASIC also supports greater standardisation of definitions of key terms. This is expected to improve consumer outcomes by minimising the likelihood of consumer confusion.

A The limitations of disclosure

Key points

Evidence shows that disclosure documents do not improve consumer decision-making, help with product comparisons or prevent consumers buying unsuitable products.

Insurers must therefore go beyond ‘innovative disclosure’ initiatives and integrate product design, sales and marketing processes to improve consumer understanding and outcomes.

Rationale for ASIC’s approach to disclosure

- 10 In ASIC’s view, while disclosure is important, generally too much weight is put on disclosure to address problems it alone cannot fix, including those resulting from competition failures, misaligned incentives and poorly designed products.
- 11 If well designed, disclosure can, for example, contribute to market transparency and efficiency, provide information that is valuable to the private sector and to regulators, facilitate innovative development of private sector applications or tools, and act as a post-purchase reference document for consumers in the event of a dispute.
- 12 However, we do not consider it is sufficient on its own to protect consumers or drive competition in insurance. Disclosure should be complemented by the development and use of more effective regulatory tools.

Evidence of the limitations of disclosure

- 13 There is now a strong body of evidence concluding that mandatory disclosure documents (including even shorter, graphic or ‘improved’ disclosures) do not generally enhance consumer decision-making, help consumers to make real-time comparison of products and services to their benefit, or prevent them from actively avoiding unsuitable products.

Note: See, for example, Omri Ben-Shahar and Carl E. Schneider, *The failure of mandated disclosure*, 159 University of Pennsylvania Law Review 687, 2011; T. Gillis *Putting disclosure to the test: Towards better evidence-based policy*, 2015, p. 47.

- 14 In ASIC’s regulatory experience:
- (a) disclosure has not been a brake or constraint on the sale of unsuitable insurance products (including products that consumers are ineligible to claim under);

- (b) disclosure has not prevented unfair sales where consumers have been unaware that they have purchased insurance products, the price of those products and/or the risks covered by the products; and
- (c) some consumers have poor or no recall of receiving disclosure documents before purchasing insurance products.

Note: See, for example, ASIC's [Report 7](#) *Consumer understanding of flood insurance* (REP 7), [Report 416](#) *Insuring your home: Consumers' experiences buying home insurance* (REP 416) and [Report 470](#) *Buying add-on insurance in car yards: Why it can be hard to say no* (REP 470).

15 Some of the limitations of disclosure that ASIC has identified that help explain these failings include the following:

- (a) *Disclosure is generalised*—It is not designed to maximise a consumer's understanding of the product as it applies to them individually and fails to account for the fact that any one piece of information is used and understood differently from person to person and situation to situation.
- (b) *Disclosure typically occurs at a time when it is unlikely to be relevant to consumer decision making*—For example, disclosure may occur after the consumer has already made the decision to purchase the product—and all forms of disclosure compete with more compelling and timely influences (e.g. sales staff, advertising and friends and family).

Note: These limitations are more pronounced when the product is sold under a general advice model, when the salesperson can promote the benefits of the product irrespective of whether it meets the consumer's needs.

- (c) *Financial products are inherently complex*—This is particularly the case where the consumer needs to assess risk, probability and the uncertain future performance of the product on the basis of limited information and with innately constrained cognitive capacity. Strategic product complexity and sales techniques (e.g. bundled products and pricing, confusing and opaque 'discounts', unclear fee descriptors) can defeat consumer attempts at understanding even simplified disclosures.

Over-reliance on disclosure and the role of the insurance sector

16 A heavy reliance on disclosure places the onus on the consumer to protect themselves and drive a fair and well-functioning insurance sector. ASIC considers that this burden on consumers is inconsistent with recognised research and knowledge about consumer behaviour and permits market conduct that is inconsistent with community expectations.

17 In general, disclosure-based approaches rely on assumptions that are at odds with how people actually do and can behave in many decision-making contexts in financial markets. These assumptions include that:

- (a) disclosure will be effective in overcoming limitations in consumer understanding and behavioural biases; and

- (b) consumers will use information optimally in a narrow instrumental sense, they are not prone to decision biases, and they have the ability to undertake complex comparisons and calculations.

18 These assumptions also fail to adequately take into account the extent to which firms with misaligned incentives can put in place supply side barriers to a fair, well-functioning insurance sector—for example, by creating or taking advantage of consumer confusion and subtly nudging consumers towards product purchases and uses that further commercial rather than consumer interests.

19 Insurers and distributors are well positioned to influence consumers and their communications are inherently more timely and compelling than mandatory disclosure documents because of:

- (a) the direct access they have to consumers;
- (b) their expertise and resources in strategic marketing/product design; and
- (c) their increasing access to and sophistication in use of consumer data.

20 In this context, it is important to increase the expectation to go beyond ‘innovative disclosure’ initiatives, and take an integrated approach to product design, sales and marketing processes to improve the understanding and outcomes of customers.

B Specific proposals

Key points

ASIC supports:

- disclosing the previous year's premium on renewal notices;
- consumer testing of different forms of component pricing disclosures to better assess consumer benefits;
- mandating that where an insurer chooses to offer products in a class of insurance subject to the standard cover regime that at least one of those products offer standard cover; and
- greater standardisation of definitions of key terms.

Disclosing the previous year's premium on insurance renewal notices and explaining premium increases

- 21 Notwithstanding the limitations of disclosure, ASIC supports disclosure of the previous year's premium on insurance renewal notices.
- 22 We consider that this would encourage competition and comparability and allow transparent price comparisons to be made by consumers. The requirement should apply to all general insurance policies that are subject to annual renewal including car and home insurance products.
- 23 The use of renewal notices to convey this information is supported by disclosure research commissioned by the Insurance Council of Australia (ICA), which found that:
- The renewal letter was the most commonly relied on source of information pre-purchase for car and home insurance policies and was almost always the highest rated information source.
- Note: See ICA, [Consumer research on general insurance product disclosures](#), Research findings report, February 2017, p. 34.
- 24 Although some insurers may elect voluntarily to display last year's premium on renewal notices, legislative change would be required to compel all insurers to do so and ensure the disclosures are made in a consistent and comparable way.
- 25 The discussion paper refers to experience in the United Kingdom where the Financial Conduct Authority (FCA) introduced new rules to increase transparency and engagement at insurance renewal. ASIC notes that in a 2015 press release, the FCA stated:
- The inclusion of last year's premium on renewal notices had the greatest impact, prompting between 11% and 18% more people to either switch provider or negotiate a lower premium when prices sharply increase.
- Note: See FCA, [FCA to require insurance firms to publish details of last year's premium](#), Press release, 3 December 2015.

- 26 As noted in the discussion paper, experience in the United Kingdom included a degree of non-compliance with the new requirements. This included a failure by some insurers to convey the information on renewal notices in a manner that drew the consumer's attention.
- 27 Given this international experience, it is important that the legislated requirements to disclose the information also specify the precise form, content and placement of the disclosures. This will better ensure that the requirement is effective and will help enforce it. It is important that consumer testing be conducted to confirm the optimal form, content and placement of the disclosures.
- 28 The discussion paper indicates that there now appears to be broad industry support for disclosure of the past year's premium and that industry has agreed to amend the General Insurance Code of Practice to require the disclosure of the previous year's premium at renewal for home insurance policies.
- 29 ASIC also supports introduction of a requirement that insurers explain premium increases when a request is received from a policyholder.
- 30 We consider that this will better inform the consumer about the underlying reasons for premium increases and help them in deciding whether to shop around for alternative policies. It may be more effective in this regard than providing the consumer with a simple reminder to shop around. ASIC is confident that the general insurance industry can overcome any practical difficulties in providing information on the reasons for premium increases.
- 31 The discussion paper indicates that the ICA supports insurers providing consumers with the reasons for premium increases.
- 32 ASIC provides the following comments in response to selected questions in the discussion paper.

Question 8. Where the previous year's premium is disclosed, should it be just the premium, or should it include taxes and charges? Should the amount of the insured value for the previous year also be disclosed?

- 33 The disclosure of the previous year's premium should take the form that best allows direct comparison with the current year's quoted premium, as well as insurance quotes obtained from other insurers. The disclosure should also include the previous year's sum insured amount.

Question 10. Would the inclusion of the sum insured and any excess along with previous year's premium on renewal notices be more appropriate than only disclosing previous year's premiums?

- 34 ASIC supports the inclusion of the sum insured and any excess on renewal notices, in addition to the previous year's premium, as this additional information should help the consumer to compare the insurance offer.

Question 11. What are the benefits and costs in mandating a link to the ASIC's MoneySmart website to be included in new quotes and renewal notices?

- 35 ASIC recommends that consumer testing be conducted to inform any decision to include a link to the ASIC MoneySmart website in new quotes and renewal notices and to help maximise the effect of such a requirement.

Disclosing component pricing

- 36 ASIC supports measures by insurers to better inform consumers of the practical strategies they could implement to address their personal risk and the extent to which doing so would reduce their insurance premiums.
- 37 Such information is needed to enable consumers to conduct a cost-benefit analysis of various risk mitigation measures. It is also needed to provide consumers with the confidence necessary to invest financially in mitigation measures in the knowledge that doing so will reduce their risks and their insurance premiums.
- 38 ASIC understands that the Financial System Inquiry recommended disclosure of component pricing to improve the transparency of general insurance pricing. The Financial Rights Legal Centre had suggested to the Inquiry that this approach could inform consumers about what effect mitigation strategies may have on their premiums.
- 39 We consider that disclosing component pricing in insurance quotes may also better inform consumers when shopping around for insurance.
- 40 ASIC suggests that further consideration is needed to assess the various costs and benefits of disclosing component prices. We think this should include consumer testing of various forms of component pricing disclosures on renewal notices and insurance quotes.

Standard cover

- 41 ASIC agrees that the standard cover regime is not achieving its intended purpose to set out the minimum requirements for prescribed types of insurance contracts. However, this is not due to shortcomings in the concept of standard cover itself. On the contrary, standard cover has the potential to deliver significant benefits to consumers. Nor is it due primarily to deficiencies in the efficacy of the current disclosure requirements.
- 42 Rather, it is the result of a deliberate decision by insurers to circumvent the regime and not offer standard cover. This is made possible by a feature of the regime that enables insurers to avoid its requirements simply by disclosing deviations from standard cover in the Product Disclosure Statement (PDS). Insurers are even permitted to make such disclosures up to 14 days after the consumer has entered into the insurance contract, in certain circumstances.
- 43 This effectively prevents many consumers from gaining the benefits of standard cover. But it also makes it unlikely that most consumers would even be aware of the existence of standard cover or that the insurance cover they have purchased may fall short of it.
- 44 ASIC considers that there is a need to strengthen the standard cover regime and to do so in a manner that is most effective in delivering the benefits of the regime to consumers.
- 45 We therefore recommend that it be mandated that where an insurer chooses to offer products in a class of insurance subject to the standard cover regime that at least one of those products offer standard cover. Products that provide standard cover should be labelled as doing so in a manner that avoids any doubt among consumers.
- 46 This approach would enable consumers to readily access the benefits of the standard cover regime and provide greater certainty for consumers while also enabling some consumers to purchase products that offer either greater or lesser cover depending on their individual circumstances and needs.
- 47 ASIC also recommends that the standard cover regime be extended to other insurance products such as gap insurance to ensure the regime reflects the wider range of product offerings now available.

Standard definitions

- 48 ASIC supports greater standardisation of definitions of key terms used in general insurance contracts.
- 49 In our view, this is likely to improve consumer outcomes by minimising the likelihood of consumer confusion.

- 50 ASIC has long supported the use of standardised definitions in insurance contracts, particularly for natural disaster risk. An early report, ASIC’s [Report 7](#) *Consumer understanding of flood insurance* (REP 7), identified that the lack of standardisation of the term ‘flood’ in home and contents insurance documents meant that consumers may not be aware whether they are covered for flood and, if they are, about the importance of the distinction between flood and other storm damage.
- 51 REP 7 recommended that insurers simplify and harmonise the drafting of insurance policies so that the availability or exclusion of flood insurance under home and home contents insurance policies was clarified. The confusion described in REP 7 was subsequently illustrated by issues that arose following the Queensland floods in 2010–11.
- 52 The discussion paper refers to industry remarks that the use of standard definitions could result in insurers offering the same cover, thereby reducing consumer choice. ASIC suggests that there is some doubt as to whether most consumers are even aware that such a ‘choice’ exists or whether it provides any genuine benefit to them.
- 53 ASIC’s [Report 416](#) *Insuring your home: Consumers’ experiences buying home insurance* (REP 416) reported the findings of an online survey which asked consumers if they read or looked at the PDS when buying home building insurance. The findings of this survey are instructive given that careful reading of PDSs would be almost essential to identifying and understanding differences in definitions.
- 54 The survey found that only two in every ten consumers (20%) who took out new insurance or considered switching did read the PDS. Even then, the accompanying qualitative research found that ‘reading’ the PDS generally meant reading selected pages, not all of it.
- 55 The findings in REP 416 suggest that consumers know very little about the details of their home insurance policy. Some consumers did not know that policies differed as they assumed that all home insurance policies were the same. They therefore asked insurers few questions about their policy and did not think it necessary to read the PDS. Unless their insurer specifically told them otherwise, these consumers did not find out that policies can differ in their caps, limits and definitions of covered events.
- 56 These findings suggest that rather than being able to take advantage of the choice offered by differing definitions, many consumers are unaware that definitions can differ. Meanwhile, the risk that consumers are taking decisions based on a mistaken belief that definitions are the same may outweigh any benefits.

Facilitating product comparison

- 57 In addition to the points made above in support of standard cover and the wider use of standard definitions, ASIC considers these reforms are also needed to better enable consumers to compare insurance products.
- 58 We are aware of calls for the introduction of a general insurance comparison website, including by the Senate Economics References Committee itself, which recommended that the Government complete a detailed proposal for an online comparison tool for home and car insurance.

Note: See Senate Economics References Committee report, [Australia's general insurance industry: Sapping consumers of the will to compare](#), August 2017, Recommendation 8.

- 59 For any such comparison website to be effective, it would need to allow consumers to directly compare like-with-like products. Consumers would also need to have confidence that the products they are comparing on the website do offer the same type of cover. If such confidence is lacking, the website may be unsuccessful.
- 60 The standard cover regime and a wider use of standard definitions would appear to represent relatively straightforward means to enhance product comparability. They are also familiar to the general insurance industry.
- 61 In this regard, we note that in its draft recommendation on a national home insurance comparison website, the Australian Competition and Consumer Commission (ACCC) identified standard cover and standard definitions as being of assistance in improving the effectiveness of such a comparison tool, as follows:

Draft recommendation 4: National home insurance comparison website

The government should consider developing a national home insurance comparison website. It should require the participation of all insurers active in relevant markets, allow consumers to compare policies by features, and make it quick and easy for consumers to act on the results.

Enhanced comparability of products, such as through standardised definitions...and mandated standard cover...will assist in the effectiveness of such a website. (emphasis added)

Note: See ACCC, [Northern Australia Insurance Inquiry](#), First interim report, November 2018, Draft recommendation 4.

- 62 ASIC recommends strengthening the standard cover regime and the greater standardisation of definitions of key terms due to the direct benefits that doing so will provide to consumers. However, we agree with the ACCC that these reforms would also help to improve the effectiveness of a national insurance comparison website, if it was established.

Review of the Key Facts Sheet

63 The Monash University research referred to in the discussion paper provides evidence about limitations on the effectiveness of Key Fact Sheets. The research examined the effectiveness of home contents PDSs and Key Facts Sheets in helping consumers to select the policy that best suited their needs.

64 The research found that:

despite ideal and simplified conditions, up to 42% of participants chose the worst offer, despite being given the time and opportunity to review the disclosure information. When able to choose from three policies, 35% chose the worse policy and only 46% found and selected the best policy. There was no simple and consistent effect of disclosure—while participants were more likely to forego purchasing an insurance policy when they had only access to the PDS the results did not find a clear pattern of understanding where people were provided more or less disclosure information. Purchasing decisions were not affected by the way in which the consumer viewed the disclosure (i.e. computer or smart phone). (emphasis added)

Note: See J. Malbon and H. Oppewal, Monash University, Melbourne, [\(In\)effective disclosure: An experimental study of consumers purchasing home contents insurance](#), research report of a study commissioned by the Financial Rights Legal Centre, 2018.

65 ASIC notes that this research is predated by the recommendation to review the utility of the Key Facts Sheets in the 2017 report by the Senate Economics References Committee into the general insurance industry.

Note: See Senate Economics References Committee, [Australia's general insurance industry: sapping consumers of the will to compare](#), August 2017.

66 The utility of Key Facts Sheets may be enhanced with the introduction of standard cover and a broader range of standard definitions.

A modern approach to disclosure

67 In considering a modern approach to disclosure, it is important to keep front of mind the risks as well as the opportunities associated with the digital forms of disclosure that are typically characterised as being ‘innovative’, with the risks more acute when firm incentives are out of alignment with their customers.

68 The potential negative impact of modern technology on attention and information processing is particularly relevant. For example, consumers interpret and engage with digital information in a different way to offline information, and process information differently across different digital devices. They process information on screens at faster speeds and can be more likely to skim read and rush their thinking.

69 This tendency can be even stronger with small devices such as mobiles. Attention can be especially short on digital devices (e.g. when people are ‘on the go’, or in a hurry), increasing the chance that rushed or shallow thinking and visual biases will affect their decisions as shown in the Monash University research.

Key terms

Term	Meaning in this document
ACCC	Australian Competition and Consumer Commission
ASIC	The Australian Securities and Investments Commission
discussion paper	Disclosure in general insurance: Improving consumer understanding , issued by Treasury in January 2019
FCA	Financial Conduct Authority (UK)
guaranteed asset protection (GAP) insurance	General insurance that covers the difference between the amount a consumer owes on their car loan and any amount they receive under their comprehensive insurance policy, if the car is a total loss
ICA	Insurance Council of Australia
inquiry	The Senate Economics References Committee Inquiry into Australia's general insurance industry
insurer	An insurance company authorised by the Australian Prudential Regulation Authority to conduct new or renewal insurance business in Australia
Key Facts Sheet	A two-page document, required by the Insurance Contracts Regulations, summarising key information about a home building and/or home contents policy
policy	The insurance contract
Product Disclosure Statement (PDS)	A document that must be given to a retail client in relation to the offer or issue of a financial product in accordance with Div 2 of Pt 7.9 of the <i>Corporations Act 2001</i> <p>Note: See s761A of that Act for the exact definition.</p>
REP 7 (for example)	An ASIC report (in this example numbered 7)