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28 February 2019

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

By email: insurancedisclosure@treasury.gov.au

Dear Sir/Madam,

Disclosure in General Insurance: Improving Consumer Understanding

The Law Society of NSW appreciates the opportunity to comment on the 'Disclosure in General Insurance: Improving Understanding' Discussion Paper ("Discussion Paper"). The Law Society's Business Law Committee contributed to this submission.

General

The Law Society supports measures to enhance the accessibility of information to assist consumers to make informed decisions about insurance products to meet their needs. It is worth noting, however, that there is no 'one size fits all' approach when it comes to general insurance, due to the varying nature of different product lines and market segments.

As liability clauses are drafted to reflect a body of case law that has defined certain terms,¹ caution needs to be taken about mandating what must or could explained in more simplified terms to consumers.

Despite the Discussion Paper's title, its focus is on personal insurances, and more specifically car and home insurance and, to a lesser extent, it also mentions strata insurance. It does not mention travel insurance, which a consumer can purchase directly, or under a group or master policy through their credit cards. Strata insurance is a special case – the insured is an owners corporation, which often relies on insurance brokers to help explain insurance cover. Small businesses also source their business insurances directly online, although many still use a broker; and in our view should also be considered in any review which focuses on improving guidance and disclosure in general insurance.

Many of the questions in the Discussion Paper require the input of industry and consumer groups, for example, regarding premium, pricing disclosure, policy coverage, for their industry-specific expertise or experience.

Our responses to some of the specific questions in the Discussion Paper are set out below.

¹ For example, "arising out of" has a different meaning to "caused by", which has a different meaning to "in connection with".

Consultation questions

Premium increases and component pricing included in renewal notices

- 1. It has become apparent from discussion with industry stakeholders that there is no generally accepted definition of component pricing. What is understood by the term 'component pricing'?**

Component pricing can refer to a range of pricing disclosure models, for example package policies e.g. a home package which has different sections on building and contents covers. While this is predominantly a matter for industry, we note that the Senate Economic Reference Committee defined component pricing at an individual product level as "breaking a premium down into broad factors such as the base premium, taxes, cyclone and flood components".²

- 2. What is the goal of disclosing a breakdown of an insurance premium on renewal notice (component pricing)? How would consumers use this information?**

The goal of such disclosure is aligned with the objective of the current disclosure regime set out in the *Corporations Act 2001*, which is to provide information that "a person would reasonably require for the purpose of making a decision, as a retail client, whether to acquire the financial product."³ Component pricing would allow consumers to take action to mitigate risks that are increasing their premiums, for example, measures to protect the property against floods or implementing security measures, such as installing alarm systems.

Consumers should receive better information, not necessarily more information. We consider that in many cases, setting out the base premium, stamp duty, GST, and any relevant levies, for example an emergency services levy (in NSW), or a fire services levy (in Tasmania), will be sufficient. Ultimately the overall price is an important factor to consumers (along with the terms of cover and the claims paying record of the insurer). If two insurers charge a premium of \$1,000, with one insurer charging \$400 for a building section and \$600 for a contents section, and another insurer \$450 for a building contents section and \$550 for a contents section, the different split seems of little practical use to consumer.

However, other information, such as flood and cyclone components in the case of home insurance, and commissions payable to strata managers on strata insurance quotations may be highly relevant. It has been suggested that this information would provide 'a signal to consumers of the risk factors taken into account when premiums are set'.⁴

- 3. Are there any risks associated with insurers providing a detailed breakdown of a premium's components (i.e. commercial sensitivities)?**

Insurers have different claims' experience, underwriting criteria, price rating structures, commission/salaries/overhead/reinsurance expenses and return on equity requirements. Why one insurer charges \$X may not therefore be comparable to another charging \$Y. There is an IT cost in providing a detailed breakdown of a premium's components. As stated above, some of this information appears to be of little practical use to a consumer, while some of the information is highly useful. We submit that any component that is

² Senate Economic Reference Committee, August 2017, *Australia's general insurance industry: sapping consumers of the will to compare*, 33 available at: [file:///C:/Users/ljb/Downloads/report%20\(9\).pdf](file:///C:/Users/ljb/Downloads/report%20(9).pdf)

³ *Corporation Act 2001*, ss. 1013D (1).

⁴ Discussion Paper, 11.

easily ascertainable by an insurer and not subject to commercial sensitivities, should be disclosed.

- 4. If consumers act to mitigate some of the risks broken down in component pricing disclosure, how would insurers reduce their premium?**

This is not a matter that we can comment on.

- 5. Would the disclosure of component pricing on policy renewal notices be appropriate for any other type of general insurance product other than home building and home contents insurances?**

As component pricing helps consumers mitigate against risks that increase premiums, we consider that it could be useful for other types of insurance products. But as we noted above, there is no "one size fits all" approach to general insurance and this question should be considered on a product-by-product basis.

- 6. What components would be most useful for consumers to see listed on their renewal notices? (For example taxes, amount attributable to flood cover?)**

See our answers to questions 2 and 3 above.

- 7. What data/breakdown are insurers able to provide if component pricing disclosure was introduced?**

This is a matter for insurers.

- 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?**

We consider that taxes and charges should be disclosed in addition to the previous year's premium. The amount of the insured value should also be disclosed, as a number of factors such as inflation, the aggregation of new assets or otherwise, may result in an increase in the insured value.

- 9. Would insurers prefer to provide further information along with a breakdown of component pricing (for example, a written explanation in the renewal notice, the opportunity to call their contact centre for more information)? Would these items be helpful for consumers?**

We cannot answer as to the preference of insurers. We suggest that a written explanation in the renewal notice and/or the opportunity to contact the insurer through the provision of relevant contact details, for example email and telephone details, would be helpful for consumers.

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

Yes, we support including the sum insured and any excess along with the previous year's premium. The sum insured may increase from the previous year as noted in our response to question 8. Similarly, the deductibles and excess may change, so it would be useful to also include this information.

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?

We consider that this would provide a benefit. The Discussion Paper notes that the Australian Competition and Consumer Commission's First Interim Report recommended inclusion of a link to ASIC's MoneySmart website on new quotes and renewal notices. This recommendation is consistent with the Insurance Council of Australia's research findings that renewal notices are the most commonly relied upon source of pre-purchase information for car and home insurance.⁵

There is an IT cost, however, which would ultimately be borne by consumers, which must be factored into any cost/benefit analysis.

12. Are there any risks associated with disclosing the types of costs that count towards estimation of sum insured?

We have no comments.

13. Would the disclosure of types of costs that count toward sum insured on insurers' sum insured calculator be appropriate?

We have no comments.

Standard Cover

14. Does standard cover achieve the purpose for which it was implemented? If not, how could it be improved?

We consider that the standard cover regime is no longer fulfilling its intended purpose. The regime was intended to provide consumers with a product that provided a basic level of cover that they could use as a benchmark to compare with other policies. However, as noted in the Discussion Paper, a contract can deviate from standard cover so long as the consumer was clearly informed, knew, or ought to have known.⁶ Currently, this requirement is met by supplying the consumer with a product disclosure statement ("PDS") that discloses the deviation from standard cover. However, as the deviation does not need to be highlighted, and research has shown that PDS's are not frequently read,⁷ this disclosure is not effective. As a result, the standard cover regime has failed to provide the level of disclosure required to enable consumers to make informed decisions when purchasing insurance.

We suggest that consumer understanding of the policy coverage could be improved by standardising definitions and key policy terms which would allow consumers to focus on price, insurer claims paying record, recent product claims or loss ratio, insurer claims paying ability per ratings agencies and insurer contact points for consumer queries before buying the policy or at claims time or other customer service points.

It may also assist product comparability if insurers are required to publicise their claims service history through ratings agencies. As insurance is essentially about paying valid claims promptly, ratings seem useful for consumers and can be provided in a short and easy to understand format.

⁵ Discussion Paper, p10.

⁶ *Insurance Contracts Act 1984* (Cth), section 35 (2) and Discussion Paper, p13.

⁷ Insurance Council of Australia's Effective Disclosure Taskforce, *Too Long; Didn't Read: Enhancing General Insurance Disclosure*, October 2015, pp17-20.

15. Are the current terms and conditions, included caps, limits, and exclusions included under standard cover seen to be adequate?

We refer to our answer to question 14 above. As to the adequacy of caps, limits and exclusions, this is a matter for consultation with industry and consumer groups.

16. What would be the likely consequences if the standard cover regime was extended to cover a wider number of terms and conditions? What sort of areas might be usefully added to standard cover?

If the efficacy of the standard cover regime could be improved, as discussed above, then there would be benefits in extending it to cover whatever areas that research has indicated would most benefit consumers in terms of offering more choice and comparability.

17. Should there be a 'default cover' that insurers are required to provide without exception?

No, insurers should have a choice in quoting. Not all insurers quote on all policies.

18. Should all insurers be required to provide products that provide standard cover as prescribed in the Insurance Contracts Regulations?

No, but if products are offered for which standard cover is otherwise available and easily recognisable as providing standard cover, then the deviation from standard cover should be readily ascertainable.

19. Is the requirement to 'clearly inform' a consumer that an insurance contract provides less than standard cover as it is commonly understood, an appropriate threshold for insurers to satisfy before they are exempted from providing standard cover?

Under the current product disclosure regime, an insurer can comply with the requirement to 'clearly inform' a consumer when a contract provides less than standard cover simply by providing them with a PDS. The threshold, to be effective, must be augmented with minimum requirements for disclosure of deviations, outside of their inclusion in a PDS, in addition to the use of standardised definitions and policy terms.

Arguably, the present system provides no guaranteed minimum cover for insurance and no benchmarks for comparison. The problem is exacerbated by the inconsistent use of definitions across insurance policies.

20. Where insurers deviate from standard cover, should they be required to provide express disclaimers identifying where the policy deviates from standard cover?

Yes, see our answer to question 19.

In determining whether disclaimers could be useful, it is necessary to consider how the disclaimer is worded, where it is placed and how prominent it is in the medium in which it appears. Most consumers will not be aware of what 'standard cover' entails, without some explanation about what it means for there to be a deviation from standard cover. If the disclaimer is not prominent, it may not be read. If this becomes a prescribed disclaimer or legal notice (such as a notice under s1018A of the *Corporations Act 2001*),

it could simply add to the length of legal notices that are already required to be included in retail documentation and advertisements.

21. What disclosure requirements could the Government look into in order to reflect the intended purpose of standard cover requirement?

We suggest research and consumer testing is required to test the efficacy of proposed new disclosure requirements.

Standardised definitions of key terms

22. Has the standard definition of flood reduced the number of complaints/disputes with insurers about coverage?

We do not have access to the relevant data. However, we strongly support the increased use of standard definitions, while acknowledging that there are challenges in developing standard definitions in some cases.

23. Should the Government mandate standardised definitions for a menu of key terms?

Yes. The Discussion Paper states that the Australian Securities and Investments Commission ("ASIC") recommends standardising policy terms and risk factors by considering legislative changes or specific authorisations.⁸

24. If key terms were to be standardised, what definitions should the Government prioritise? What terms tend to be subject to dispute due to misunderstandings of meaning?

We suggest a list of definitions should be compiled in consultation with insurers, reinsurers, regulators and consumer groups.

25. What impact would standardising some definitions have on underwriting?

We defer to the expertise of underwriters on this issue.

We suggest, however, that case law, over time should assist with the interpretation of any standard definitions. Any statistics published by the Australian Prudential Regulation Authority ("APRA") in relation to claims may also be more easily comparable.

26. Should there be standard definitions for exclusion, for example, wear and tear?

Yes, especially for terms which have an accepted meaning within the insurance industry or which have been the subject of case law.

Review of the Key Facts Sheet

27. Should the KFS be extended beyond two pages to convey more information, similar to the short-form PDS?

We advocate for consumer testing for any changes proposed to the Key Fact Sheets ("KFS"). The main emphasis should be on increasing the utility of KFS's in improving consumer understanding of home building and contents policies. Whether the KFS

⁸ Discussion Paper, p17.

should evolve into a short form PDS depends on what should be included in a KFS/short form PDS, and whether there is a risk that a short form PDS could result in consumers reading only the short form and not the full form PDS.

28. The form of the KFS is currently prescribed in the law, should this be removed to allow industry to take a more innovative approach?

No, since the purpose of the KFS is intended to be for comparison of policies, our view is that it is better to have a standard form to allow easy comparison.

29. Are there any legal issues industry would like to raise regarding the extension or modification of the KFS?

Not in addition to the above.

30. Are there items that would be more suitable for inclusion for consumers in a KFS?

Consideration could be given to including information provided by the insurer on the five most typical claims made and paid and those not paid plus the claims or loss ratio in the last financial year. There is a risk, however, that this information could be misleading if not accompanied by explanatory material. It can also be subject to factors such as portfolio management. There should be little cost for insurers in providing a claims or loss ratio as such information is produced for their financial statements and for APRA reporting.

31. In the context of home building and home contents insurance, what are considered to be the key policy elements that consumers need to know about for them to make an informed decision when comparing across policies?

See our answers above.

32. Would there be merit in extending the KFS requirement to other forms of general insurance? What value does it add for the consumers?

Yes, we suggest that the KFS requirement could be extended first to motor and then over time to travel, sickness and accident and consumer credit. It would be necessary first to address the identified deficiencies in the KFS's, including oversimplification of policy terms and low consumer awareness. KFS's can provide an additional tool for assessing policies together with the renewal notice and inquiry access to insurer staff and online quotes.

33. How can the low awareness of KFS's be addressed and the difficulty of consumers in comparing different policies using KFS's overcome?

The PDS could ask consumers to read the KFS in its first 100 words. Standardised definitions may assist consumer choice and comparability.

34. Should the KFS be replaced with a new approach? If so, what approach should be taken?

We consider that KFS's can still play a useful role as part of a suite of tools to assist consumers to understand their policies and to assist them to compare policies.

A modern approach to disclosure

35. Are there more effective or innovative ways to communicate information on policies to consumers?

Yes, we consider industry should utilise all platforms, including podcasts and websites to communicate information on policies to consumers.

36. Is the law currently preventing more effective methods of disclosure? If so, how?

Yes, we understand that ASIC considers that legislative change is required to remove the current restrictions to electronic disclosure in the *Insurance Contracts Act 1984* and the *Corporations Act 2001* and is currently working in consultation with the industry and Treasury on this issue.⁹

37. How could the law facilitate new methods of disclosing the content currently required in the PDS, while still ensuring adequate consumer protections?

See our answer to question 36 above.

Hayne Report

The Discussion Paper seeks stakeholder views on the Senate Committee's recommendations in relation to the disclosure regime in the insurance sector.¹⁰ The Senate Committee and Discussion paper contain information from the relevant reviews and inquiries which have preceded the current consultation. Since the publication of the Discussion Paper, the Final Report of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry has been published. Commissioner Hayne has made a number of recommendations that may also have an impact on the disclosure regime for insurance contracts, particularly recommendation 4.7-Application of unfair contract terms provisions to insurance contracts and recommendation 4.9- Enforceable code provisions.¹¹

The Law Society supports, in principle, the recommendations in the Final Report relating to the insurance sector.

If you have any questions about this submission, please contact Liza Booth, Principal Policy Lawyer, at liza.booth@lawsociety.com.au or on (02) 9926 0202.

Yours faithfully,



Elizabeth Espinosa,
President

⁹ Senate Economics References Committee, above n 35-36.

¹⁰ Discussion Paper, p 2.

¹¹ Commonwealth, Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry, *Final Report* (2019) Vol 1, 32-33.