

29 March 2019

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

By Email: claimshandling@treasury.gov.au

Dear Sir/Madam,

ISA Response - Insurance Claims Handling Treasury Consultation

Industry Super Australia (ISA) appreciates the opportunity to provide comment on the Insurance Claims Handling Treasury consultation paper (**Consultation Paper**), the purpose of which is to implement the Government's response to recommendation 4.8 of the Final Report of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry (**Final Report**).

Commissioner Hayne recommended that:

“The handling and settlement of insurance claims, or potential insurance claims, should no longer be excluded from the definition of financial advice”¹.

In response to the recommendation the Consultation Paper proposes:

1. the removal of Corporations Regulation 7.1.33; and
2. that existing legislative powers be used to define the activity of handling or settling an insurance claim as a “financial service” for the purposes of the Corporations Act. The definition could be enacted in primary legislation or regulations.

Removal of Regulation 7.1.33

Regulation 7.1.33 of the Corporations Regulations carves out the handling and settlement of insurance claims, or potential insurance claims from the definition of “financial advice”. The effect of this is that some of the general (but important) obligations in section 912A of the Corporations Act do not apply to claims handling. For example, the requirement to handle and settle claims efficiently, honestly and fairly, does not apply to insurance claims. As ASIC rightly pointed out in its policy submission:

¹ Final Report, Royal Commission into Misconduct in the banking, Superannuation and Financial Services Industry, Volume 1, p 33.

“For consumers, the intrinsic value of an insurance product lies in the ability to make a successful claim when an insured even occurs”².

The current carve out disadvantages consumers and has caused significant harm, as evidenced by the case studies³ before the Royal Commission. There is a need for regulatory reform to protect claimants and potential claimants from the activities of insurers that are not efficient, honest or fair or are otherwise inconsistent with the general obligations in section 912A of the Corporations Act.

The grounds for the existing carve out are opaque and appear to be a concession to claims that regulatory oversight would add costs to the system whilst providing no benefit to consumers. Such concessions can no longer be accepted.

Additionally, the removal of the exemption ensures that all activities involved in the handling and settlement of an insurance claim are a financial service and subject to regulatory oversight (i.e. ASIC oversight). ISA supports this approach.

The financial services industry can no longer support such a disadvantageous exemption for consumers. As Commissioner Hayne observed in his Final Report:

“There can be no basis in principle or in practice to say that obliging an insurer to handle claims efficiently, honestly and fairly is to impose on the individual insurer, or the industry more generally, a burden it should not bear. If it were to be said that it would place an extra burden of cost on one or more insurers or on the industry generally, the argument would itself be the most powerful demonstration of the need to impose the obligation. The argument can be made only if claims handling is not now conducted efficiently, honestly and fairly. And if that is the case, it should no longer be tolerated by the industry or by the law.”⁴

ISA supports the removal of regulation 7.1.33, which will give effect to recommendation 4.8 of the Final Report.

Definition of the handling and settlement of an insurance claim as a financial service

The Consultation Paper suggests that existing legislative powers could be used to define the activity of handling or settling an insurance claim (in relation to both general and life insurance products) as financial services for the purposes of the Corporations Act. While a specific definition has not been put forward and further consultation would be required, in principle ISA supports the introduction of a revised definition of financial services incorporating the activity of handling or settling an insurance claim. The definition should cover all policyholders, claimants and potential claimants.

The introduction of such a definition should ensure that there is clarity about which activities (whether directly or indirectly) are caught by the requirements of the Corporations Act and in doing so ensure the level of consumer protection is adequate.

² ASIC, Module 6 Policy Submission, 27

³ Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry, Final Report, Volume 2: Case Studies pp 289-455

⁴ Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry, Final Report, Volume 1 page 308

However, the Consultation Paper does not adequately address the following key matters, which go to the requirement to handle and settle claims efficiently, honestly and fairly:

1. Timeframes for consideration of a claim: central to many consumer complaints concerns delays in claims consideration and payments.
2. Asymmetry in information: ineffective or a lack of information provided to claimants and potential information is a key concern and disadvantageous to consumers.

Whilst these are matters could be classified as sub-issues within any general requirement to act efficiently, their importance to the consumer experience is such that these matters should be explicitly addressed.

We note the claims timeframes and obligation to provide claimants and potential claimants with information to assist in the claims processes are contained in the Financial Services Council's Life Insurance Code of Practice and the Insurance in Superannuation Code of Practice. These codes are currently voluntary but introduce a much-needed level of efficiency and fairness into the system.

Option to exempt certain documents relating to claims handling

Page 11 of the Consultation Paper raises the prospect of altering subsection 766B(1A) of the Corporations Regulations to include claims handling documents or statements as exempt statements and therefore not constituting financial product advice. [Emphasis added] This is a matter that requires further clarification and consultation.

ISA does not oppose measures which ensure that there are not any unintended consequences flowing from the removal of the claims handling exemption. However, it is equally important to ensure that there are no unintended reductions in protections to consumers as a result of any expansion of the scope of s766B(1A) of the Corporations Act.

Scope of proposal

ISA supports a broad application of the proposed changes to ensure that all policyholders are covered by the definition of handling or settling of insurance claims. In addition, the scope of the changes should not only apply to insurers, but to all those with decision making authority over claims, including agents. The proposed changes to insurers are not inconsistent with the obligations already imposed upon superannuation trustees.

The majority of life and disability insurance held in Australia is held by superannuation trustees on behalf of their members. Group insurance purchased by trustees is cost effective with levels and types of cover adapted to suit the demographics of the members of the superannuation fund.

Superannuation trustees do not supply insurance products directly to their members, rather they are obliged to purchase minimum levels of insurance on behalf of their members⁵, or in certain circumstances not to purchase insurance on their behalf.

⁵ Section 68AA of the Superannuation Industry (Supervision) Act 1993 requires trustees to take out permanent incapacity and death benefit insurance covering MySuper members on an opt out basis. Recent changes introduced as part of the Protecting Your Super legislative reforms prohibit the offering of insurance to certain cohorts of members.

Superannuation trustees have statutory and common law duties, which include an obligation to act in the best interests of their members. The unique role of trustees enables and requires them to support members of their fund through the claims process.

The covenants included in section 52 of the *Superannuation Industry (Supervision) Act 1993 (SIS Act)* impose particular obligations, including those specifically relating to insurance in section 52(7).

Sub-section 52(7)(g) of the SIS Act requires trustees “*to do everything that is reasonable to pursue an insurance claim for the benefit of a beneficiary, if the claim has a reasonable prospect of success.*”

Insofar as it is possible, ISA has no objection to changes relating to insurance claims handling and settling applying to superannuation trustees and others who have a role in the settlement and handling of insurance claims, including third party agents. However, it should be recognised that superannuation trustees are the policyholders, not the issuer of the policy.

Trustees do have responsibilities to assist their members in the handling and settlement of insurance claims and an overarching obligation to design and purchase insurance arrangements that are best suited to the demographic of the members of the fund.

Why claims handling is important

At the time of making a claim an insured person and or their family is often in a period of stress. During these difficult times consumers rightly expect to receive assistance and empathy. It is a reasonable consumer expectation that they should be able to readily make a claim when an insured event occurs and a community expectation that during the claims handling process insurers and their representatives treat claimants and potential claimants with compassion and respect. Importantly this includes assisting claimants to navigate their way through the claims process. It is also a reasonable expectation of claimants that ‘their insurer’ will aid rather than hinder. The Royal Commission heard evidence of failures to handle claims in a fair and transparent manner, delays in the processing of claims and other instances where there was a failure to have systems in place, including systems to avoid conflicts of interest.⁶

Consumers are purchasing insurance with the expectation, an expectation encouraged by insurer advertising, that claims will be speedily and appropriately handled. Where claims handling outcomes fail to meet the proposed requirements there should be ramifications for insurers, including penalties and the potential loss of license.

Industry Code of Practice

ISA welcomes the development of the Financial Services Council’s Life Insurance Code and the Insurance in Superannuation Code of Practice, including the adoption of timescales for the claims process and requirements to provide certain information to claimants.

⁶ Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry, Final Report, Volume 2: Case Studies pp 289-455

Consultation questions

1. **Are there additional issues that have not been identified? If so, are there potential options for addressing them within the proposal?**

The issue of information asymmetry has not been addressed in the Consultation Paper. For an insured person to make and follow through a claim they must understand their rights and entitlements.

Readily understood consumer information relating to the claims process empowers consumers. There is little incentive for insurers to invest in empowering those who may make claims against it. It is noted that the FSC Insurance and Insurance in Super voluntary codes of practice recognise the importance of providing key information to consumers that assists the efficient claims handling process.

Further consultation is required regarding the scope of the application of AFSL licensing requirements to the insurance sector, in particular its potential application to compulsory motor or workers compensation insurance.

2. **Are there other approaches that can be taken in designing the legislative amendments that would further improve consumer outcomes (including by reducing compliance costs)?**

The current proposals are supported. It is also noted that there is a concurrent consultation process regarding the merits of mandating currently voluntary codes of practice, including providing powers of enforcement by ASIC. The claims handling components of codes applicable to the insurance industry may be impacted by these proposals as may the mandating of existing codes. These matters should be considered concurrently.

3. **Are there any obligations, besides the existing AFS licensing obligations, that would provide further useful consumer protections in respect to claims handling activities and so should also apply to them?**

In addition to contract law and the Corporations Act there is a range of law that governs the insurance industry, including the *Insurance Act 1973* the *Insurance Contracts Act 1984* and the *Privacy Act 1988*.

ASIC's oversight of the insurance industry is not as limited as understood and extends beyond licensing obligations. These powers include the general powers under Division 2 of the *Australian Securities and Investments Commission Act 2001*. Ultimately the licensing powers are the largest stick in ASIC's armoury.

In August 2018 after releasing ASIC's report 587 – The Sale of Direct Life Insurance, ASIC Chair James Shipton stated in a media release:

“ASIC will use all of its regulatory tools to address failures in this market – including through enforcement action and policy reform. We have several investigations underway.”⁷

⁷ <https://asic.gov.au/about-asic/news-centre/find-a-media-release/2018-releases/18-250mr-asic-s-review-of-direct-life-insurance-finds-high-cancellation-rates-and-poor-claims-outcomes/>

Industry codes of practice are of some benefit, particularly those monitored by the Australian Financial Complaints Authority's Code Compliance and Monitoring team.

“The introduction of the Code by the FSC appears to have played a role in improving sales standards. However, significant improvements are still needed to reduce the risks of poor consumer outcomes and to consistently place the interests of consumers at the centre of the direct life insurance market, and to increase consumer trust in direct life products and how they are sold.”⁸

The proposed changes to remove the claims handling exemption will assist in the resolution of some of the problems identified.

4. How could the activity of handling or settling an insurance claim (in relation to both life and general insurance products) be defined as a financial service for the purposes of the Corporations Act?

The definition of handling and settling of claims should be as broad and as simple as possible. A possible definition could be:

“All processes, actions and systems involved in the handling and settlement of claims and potential claims.”

The definition of handling or settling of insurance claims should include ways in which an insurer or its representative makes a decision about a claim, including:

- investigating and assessing claims;
- interpreting policy provisions;
- conducting settlement negotiations;
- preparing loss estimates or repair costs; and
- recommendations regarding mitigation of loss.

It is envisaged that these obligations would ordinarily include:

- the management of conflicts of interest;
- the dedication of appropriate resources for training and supervision;
- compliance with laws and licence conditions;
- risk management systems; and
- appropriate external and internal dispute resolution systems.

The definition of the handling and settlement of claims as a financial service should ensure it encompasses potential claimants and that efficiency requirements include the provision of adequate and accessible information to consumers.

5. What penalties should apply to insurers breaching the general obligations of s912A in the specific instance of insurance claims handling? Should the penalties attaching to insurance claims handling, be the same that attach to other financial services?

It would be appropriate that the penalties that apply to breaches of other financial service obligations also apply to claims handling related breaches. There is sufficient discretion available to apply appropriate penalties proportionate to the nature of and circumstances surrounding breaches.

⁸ ASIC Report 587: Sale of Direct Life Insurance <https://download.asic.gov.au/media/4852974/rep587-executive-summary-published-30-august-2018.pdf>

Thank you for the opportunity to provide feedback on the Insurance Claims Handling consultation paper. Please do not hesitate to contact me if you have any further questions.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Richard Watts', with a stylized flourish at the end.

Richard Watts
Consultant