

26 February 2025

Director
Programs and Redress
Unit Financial System Division
The Treasury
Langton Crescent
PARKES ACT 2600

By email: CSLRreview@treasury.gov.au

Dear Director

Post-Implementation Review: Compensation Scheme of Last Resort (January 2025)

The Insurance Council of Australia (Insurance Council) welcomes the opportunity to provide a submission to Treasury's 'Post-Implementation review: Compensation Scheme of Last Resort' (CSLR) (the review').¹

The Insurance Council is the representative body of the general insurance industry in Australia and represents approximately 90 per cent of private sector general insurers. As a foundational component of the Australian economy, the general insurance industry employs approximately 60,000 people and on average pays out \$147 million in claims each working day (\$36.5 billion per year).

The Insurance Council welcomes the review of the CSLR to ensure it is sustainable into the future. In line with the terms of reference for the review, our submission comments on if the CSLR is delivering on its intended objectives, the impact of the funding model and current scope.

The Insurance Council supports the role of the CSLR to act as a genuine scheme of last resort which provides victims of financial misconduct an avenue for redress and compensation, when all other avenues have been exhausted. The top ten financial institutions by income, including insurers, paid an upfront levy to the CSLR of approximately \$241 million to fund the costs of addressing the backlog of in-scope complaints that accumulated with the Australian Financial Complaints Authority (AFCA) between 1 November 2018 and 7 September 2022.²

To ensure that the CSLR is meeting its intended purpose and is sustainable in the long-term, we recommend:

1. The current scope of the CSLR is not expanded and consideration be given to the scope of the funding model. Currently, there is a Ministerial 'special levy' to be collected from a specified sub-sector (such as general insurers) in circumstances where the estimated costs for one or more in-scope sub-sectors exceeds that sub-sector levy cap. As outlined below, we do not support cross-subsidisation which essentially requires companies that meet expected ethical and prudential standards to underwrite those who do not.
2. The funding model be reviewed to consider any risks of inadvertently discouraging subsectors that have created losses to uplift their standards and prevent future consumer harm. We believe

¹ Treasury (January 2025), '[Compensation Scheme of Last Resort post-implementation review](#)'.

² [Compensation Scheme of Last Resort Impact Report 2024](#)

that ongoing uplift that prevents future consumer harm is crucial to long-term sustainability and viability.

3. The CSLR is supported by frameworks that help to mitigate against and address underlying issues within in-scope sectors, to help avoid significant stress and anxiety for Australian consumers and potential losses in the first instance.
4. In reviewing the operation of the 'special levy' element of the funding model, careful consideration is given to potential impacts on the affordability of insurance if a special levy is imposed on the insurance sector, which would increase further cross-subsidisation of the scheme.
5. AFCA's approach to determining compensation amounts is reviewed against the CSLR's intended purpose.

Intended objectives

As noted in the review, the CSLR objectives are to:

- Support confidence in the financial system's external dispute resolution framework.
- Provide some compensation for victims of financial services misconduct as a last resort where a determination issued by the Australian Financial Complaints Authority remains unpaid and the determination relates to a financial product or service within the scope of the scheme; and
- Be sustainable over time and funded by an industry levy.

The 'but for' compensation principle applied by AFCA in determining in-scope complaints in an investment advice scenario evaluates the financial position a complainant would have been in if the misconduct or inappropriate advice had not occurred. We note this is compared to an alternative investment strategy which is applied retrospectively and provides consumers with compensation where they may not have made loss. AFCA's approach to determining compensation by applying a 'but for' principle appears to have increased the overall cost of the CSLR.³

This outcome does not appear to align with the intended objective of the CSLR outlined above. As a result, we recommend AFCA's approach to determining compensation amounts is reviewed against the CSLR's intended purpose.

Funding model and cross-subsidisation

The top ten financial institutions by income, including insurers, paid an upfront levy to the CSLR of approximately \$241 million to fund the costs of addressing the backlog of in-scope complaints that accumulated with the Australian Financial Complaints Authority (AFCA) between 1 November 2018 and 7 September 2022.⁴ However, we have concerns over the financial sustainability of the CSLR to provide a last resort for victims of financial services misconduct.

The expenditure of the CSLR is difficult to estimate as it depends on future events, such as financial firm failures, which give rise to a 'randomness' in outcomes.⁵ This uncertainty is exacerbated by the

³ See Australian Financial Complaints Authority webpage, '[Compensation Scheme of Last Resort](#)' and AFCA Approach Document, '[Determining compensation in complaints against Financial Advice Firms where the Responsible Entity of a Managed Investment Scheme has become insolvent](#)'.

⁴ [Compensation Scheme of Last Resort Impact Report 2024](#)

⁵ [Initial Estimate for 2025/26 \(3rd Levy Period\)](#), page 4, Section 1.5.

escalating costs arising from complaints in relation to the collapse of financial advice firms.⁶ The CSLR operator has advised that for levy period 3 (2025-26), the CSLR will exceed the \$20 million cap for the financial advice subsector.⁷ This could impact levy arrangements in future years or trigger the implementation of a 'special levy' on other sectors after 1 July 2025. We understand a special levy may be necessary to raise additional funds due to an expected shortfall in funding for the financial advice sector of over \$50 million.⁸

This 'special levy', a built-in mechanism for cross-subsidisation, has been described as necessary to ensure appropriate compensation for 'black swan' events. Unfortunately, collapses of non-prudentially regulated financial services firms are occurring on a more regular basis. Where similar incidents occurred in prudentially regulated industries, the Government has been able to review supervisory and prudential standard to prevent further collapses and protect consumers in subsequent years.

The regulatory framework should be designed to minimise calls on the CSLR. From a customer perspective, it is preferable for regulatory supervision to prevent such collapses rather than seek to remedy them after they occur.

We believe that any application of the special levy must not inadvertently discourage the subsectors that have created the losses to uplift their standards and prevent future consumer harm. We welcome clarification on what sub-sectors, such as insurance, may be subject to any consideration of an upcoming special levy.

The Insurance Council recommends that the current scope of the CSLR should not be expanded, and consideration be given to the scope of the funding model, particularly on the application of the cross-subsidising nature of the 'special levy'. This would include further clarification on the process for applying the special levy and identifying contributing sub-sectors.

The ongoing sustainability of the CSLR would be enhanced through other frameworks that help to mitigate against and address underlying issues within sectors first, as opposed to a focus on the remediation process, to help avoid significant stress and anxiety for consumers.

Affordability of insurance

The industry understands that insurance affordability stress is a growing issue of concern. The Actuaries Institute previously estimated that 12 per cent of all Australian households were under home insurance affordability stress, defined as the cost of home insurance being greater than four weeks of gross household income (whether insurance was purchased or not).

The increasing frequency and severity of extreme weather in Australia is exacerbating this concern. To address insurance affordability in the short to medium term, the industry is focusing on strengthening the resilience of communities and businesses to better withstand the disasters Australia is already facing. The industry is actively engaging with governments and regulators including the Australian Government's Hazards Insurance Partnership (HIP), on measures that focus on risk reduction and community resilience. Insurers are also partnering with the Australian Prudential Regulation Authority (APRA) to conduct a Climate Vulnerability Assessment, focusing on how a warming climate impacts general insurance availability. We recognise that these measures will take time to implement.

⁶Australian Financial Complaints Authority (AFCA), [Compensation Scheme of Last Resort](#)

⁷ [Initial Estimate for 2025/26 \(3rd Levy Period\)](#).

⁸ The *Corporations Act 2001* (Cth), Section 1069H(5)(b).

The insurance industry has navigated through a significant period of regulatory change in recent years. This includes an increasing number of new laws and regulations flowing from recommendations of the Hayne Royal Commission, often resulting in complex frameworks.

In reviewing the operation of the 'special levy' element of the funding model, we recommend careful consideration is given to potential impacts on the affordability of insurance if a special levy is imposed on the insurance sector, which would increase further cross-subsidisation of the scheme.

Conclusion

We look forward to the outcome of Treasury's review and would welcome the opportunity to discuss our submission further.

If you have any questions related to our submission, please contact me or Leisha Watson, Director Regulatory and Consumer Policy at watson@insurancecouncil.com.au.

Yours sincerely



Alexandra Hordern

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