INSURANCE COUNCIL OF AUSTRALIA

Mr Scott Rogers
Manager, Consumer Policy Unit
The Treasury
Langton Crescent
PARKES ACT 2600

By email: Scott.Rogers@treasury.gov.au

29 February 2016

Dear Mr Rogers

EXEMPTING MARINE INSURANCE CONTRACTS FROM SMALL BUSINESS UNFAIR CONTRACT TERMS LAW

The Insurance Council of Australia[1] (the Insurance Council) is writing in response to the Treasury's recent invitation to apply for an exemption of marine insurance contracts governed by the *Marine Insurance Act 1909* (MI Act) from the Government's Small Business Unfair Contract Terms Law (Small Business UCT Law).

The Insurance Council would like to thank the Treasury for the guidance provided regarding the formal application process. This has been invaluable in helping ensure that the Insurance Council provides the appropriate information for consideration by the Minister for Small Business and Assistant Treasurer.

The Insurance Council understands that, before a nominated law is prescribed, the Minister must be satisfied that it provides equivalent and enforceable protections for small business, taking into consideration: any detriment to small business; the impact on business generally; and the public interest. We also understand that the Minister's decision will also be made in the context of any requirements stipulated by the Intergovernmental Agreement for the Australian Consumer Law and Corporations Agreement 2002.

The Insurance Council supports the policy goals behind the Government's Small Business UCT Law. However, we submit that this law should not apply to marine insurance contracts regulated under the MI Act because of the potential detriment to business and consumers. The MI Act is a codification of marine law that is practised globally in a consistent manner. To depart from consistency without good reason runs the risk of inefficiency and confusion.

---

[1] The Insurance Council of Australia is the representative body of the general insurance industry in Australia. Our members represent more than 90 percent of total premium income written by private sector general insurers. Insurance Council members, both insurers and reinsurers, are a significant part of the financial services system. September 2015 Australian Prudential Regulation Authority statistics show that the private sector insurance industry generates gross written premium of $42.8 billion per annum and has total assets of $121.3 billion. The industry employs approximately 60,000 people and on average pays out about $115.6 million in claims each working day.

Insurance Council members provide insurance products ranging from those usually purchased by individuals (such as home and contents insurance, travel insurance, motor vehicle insurance) to those purchased by small businesses and larger organisations (such as product and public liability insurance, professional indemnity insurance, commercial property, and directors and officers insurance).

Most significantly, the majority of insurance contracts under MI Act issued by the Australian insurance market incorporate standard form wordings known as Institute Clauses, developed by the Lloyd's Market Association (LMA) and International Underwriting Association of London (IUA). These standard form wordings are used internationally. The uncertainty created by the wordings being open to review under the Small Business UCT Law may ultimately impact adversely on the competitiveness of the local marine insurance market.

Furthermore, as the MI Act provides an equivalent level of enforceable protections for small business from unfair contract terms, applying the Small Business UCT Law to MI Act marine insurance contracts would only create regulatory duplication and unnecessary compliance costs. We strongly consider that, in the absence of evidence of any detriment to small business or the public interest more generally, contracts under the MI Act should not be made subject to the Small Business UCT Law.

The Insurance Council therefore submits that the MI Act should be exempt under the new legislation. The Attachment sets out the detailed reasoning underpinning our application.

As this submission also concerns the operation of the MI Act, we have copied it to the Commonwealth Attorney-General's Department, which administers that Act.

If you have any questions or comments in relation to our submission, please contact John Anning, the Insurance Council's General Manager Policy, Regulation Directorate, on (02) 9253 5121 or janning@insurancecouncil.com.au.

Yours sincerely

Robert Whelan
Executive Director and CEO

cc: Ms Stephanie Ierino, Commonwealth Attorney-General's Department.

INSURANCE COUNCIL OF AUSTRALIA

ATTACHMENT

REASONS IN SUPPORT OF EXEMPTION OF MARINE INSURANCE CONTRACTS

BACKGROUND

Marine insurance contracts are regulated[2] by either the MI Act or the *Insurance Contracts Act 1984* (IC Act).

Section 15 of the IC Act currently excludes insurance contracts from the operation of a Commonwealth, State or Territory Act that provides relief in the form of judicial review of unfair contracts or the making of a misrepresentation, except for relief in the form of compensatory damages. As such, insurance contracts regulated under the IC Act are exempt from the Australian Consumer Law and the UCT protections applying to consumers. However, a similar exemption is not provided for marine insurance contracts regulated under the MI Act.

The vast majority of contracts of marine insurance issued in Australia covering the carriage of goods shipped to and from Australia incorporate the Institute Cargo Clauses (A), which is a standard form wording incorporated into insurance policies issued worldwide.

Accordingly, unless an exemption is provided, the Small Business UCT Law will apply to standard form MI Act marine insurance contracts with small business. This will create uncertainty as the standard Institute Cargo Clauses (A) wording incorporated into contracts of insurance covered by the MI Act (e.g. import and export of goods by sea) would be subject to the Small Business UCT Law, while other contracts of marine insurance covered by IC Act (e.g. inland cargo) also incorporating similar Institute Clauses, would not be subject to the Small Business UCT Law.

Possible detriment from extending small business UCT law to marine insurance

The MI Act is a codification of marine law that is practised globally and care has been taken to maintain consistency in the domestic law with well-established international practice. The Australian Law Reform Commission (ALRC), in its final report on its *Review of the Marine Insurance Act 1909*[3], explored these important considerations.

In its report, the ALRC noted that Australia has a close association with marine insurance law and practice in the United Kingdom and many other common law jurisdictions, including New Zealand, Canada, Singapore, Malaysia, Hong Kong and India, which have their marine insurance legislation derived from the United Kingdom's Marine Insurance Act (MI Act UK).

The ALRC found that the present codification of marine insurance law and practice is long established and well known and that this has contributed to a business environment in which the meaning of contracts is well understood and is backed up by comprehensive case law.

The ALRC went further to warn that unilateral changes to Australian marine insurance law may impact adversely on and isolate the Australian market by severing the association

---

[2] Insurance for inland cargo and pleasure craft is covered under Section 9A of the IC Act, while insurance for commercial hull and the transport of international cargo is subject to the MI Act.

[3] Australian Law Reform Commission 2001, *Review of the Marine Insurance Act 1909*, ALRC Report 91.

between Australian and United Kingdom law and practice, a link shared with marine insurance regimes in other common law systems and also many other countries as well.

As marine law has been long established, it is well understood by industry participants and the legal and judicial profession, both in Australia and in our overseas trading partners. This has produced consistency and certainty in the global application of marine law.

Further, as noted above, most marine insurance policies for cargo and hull incorporate standard wording Institute Clauses by reference, which form the basis of many Australian marine insurance contracts with small businesses for the import or export of cargo. Their overseas suppliers or purchasers (and their financiers) will almost inevitably require any insurance forming part of the purchase or sale price to include the applicable Institute Clauses. This helps ensure that parties to the contract have certainty over the insurance arranged by the supplying party covering the shipment. For this reason, Australian marine insurers generally must offer Institute Clauses on import/export cargo insurance.

Institute Clauses have been adopted internationally as the accepted basis of any marine insurance contract forming part of international trade terms. The clauses are published on the IUA's website and proposed amendments/new wordings are subject to a lengthy consultation process. In practice, the clauses minimise the scope for misrepresentation by insurers.

The Insurance Council is concerned that if the Small Business UCT Law applies to MI Act contracts, it will create contract uncertainty, leading to higher premiums or reinsurance charges for Australian insurers or insurers becoming more selective. The adverse economy-wide implications resulting from this could be substantial.

Principally, this would make marine insurance in Australia less attractive and diminish the international competitiveness of Australian marine insurers. In that case, marine insurance contracts for Australian risks would likely to be increasingly issued by Australia's global competitors. This would have a material flow on impact to associated domestic industries, including surveyors and other service providers appointed by insurers, as well as resulting in dispute resolution and litigation being managed in foreign jurisdictions.

As an indicator of domestic market size and potential economic impact, the total value of gross written marine insurance premium from Insurance Council members is currently worth over $0.5 billion. The Insurance Council estimates that extending the Small Business UCT Law to MI Act insurance contacts would affect around 70 per cent of the total market. While marine insurance providers generally do not collect data on the number of employees that an insured has, it is estimated that around 90 per cent of marine insurance policies are for small and medium-sized businesses, and that over 95 per cent of insurance policies have premiums at or below $300,000 in value.

As pointed out above, under some marine insurance contracts, different legislation can apply to different transit methods under the same policy, e.g. land and air transit (IC Act) versus sea transit (MI Act). In these circumstances, industry practice is for the contract to explicitly recognise that either the MI Act or the IC Act may apply through policy wording which acknowledges this – for example, disclosure provisions state that:

> "*Where the Marine Insurance Act 1909 applies, we may…*" and

"*Where the Insurance Contracts Act 1984 applies, we may*…"

One other area where this uncertainty may arise is with private/pleasure craft, which may be subject to both the IC Act and the MI Act. For instance, a charter hire of pleasure craft is expressly exempt from the IC Act under subparagraph 9A(2)(a)(ii); in other circumstances it may however be subject to the IC Act.

Our concern is that there would be a high level of uncertainty around how the Small Business UCT Law would apply to a contract in practice, given the exemption from UCT protections for IC Act contracts under Section 15 of the IC Act.

Further, the Insurance Council submits that the rationale for the operation of Section 15 of the IC Act would equally apply to the MI Act. The explanatory memorandum to the Insurance Contracts Bill 1984 states:

> "…*it is appropriate that there should be no question whether the Bill or State legislation or other Commonwealth legislation applies in a particular case and so no room for lengthy disputes as to which should apply*".

In other words, a contract of insurance should not become subject to two pieces of legislation where both are intended to govern terms of a contract. Arguably, a similar approach should be adopted with insurance contracts with small business under the MI Act.

Equivalent protection for small business

Australian small businesses that purchase marine insurance are already protected from unfair contract terms under the MI Act. Specifically, parties to a marine insurance contract are subject to duties of utmost good faith. Section 23 of the MI Act provides:

> "*A contract of marine insurance is a contract based upon the utmost good faith, and, if the utmost good faith be not observed by either party, the contract may be avoided by the other party*".

The High Court has stated that:

> "… *an insurer's statutory obligation to act with utmost good faith may require an insurer to act, consistently with commercial standards of decency and fairness, with due regard to the interests of the insured."* [4]

The duty of good faith requires the insurer and the insured to act honestly and fairly with each other throughout the duration of the policy. This duty extends to pre-contractual disclosure and non-misrepresentation, requiring that an insurer must not misrepresent facts about the policy (or any other facts) that are material to the policy. The insurer must also disclose any relevant policy terms that have major consequences.

The Insurance Council submits that the overall legal effect of this duty of good faith provides equivalent protection to small business from the potential inclusion of unfair contract terms in MI Act contracts – including unfair terms as defined under section 24(1) of the Australian Consumer Law and section 12BG(1) of the *Australian Securities and Investments Commission Act 2001*.

---

[4] *CGU v AMP* (2007) HCA 36

Reflecting the effectiveness of the duty of good faith protections, feedback from our members is that there has been no experience of any customers – small businesses or otherwise – contesting MI Act contracts due to unfair contracts terms. With no detriment to small business identified, the Insurance Council submits that extending the Small Business UCT Law to contracts under the MI Act would be unjustified.

It would always be open to the Treasury to work with the Commonwealth Attorney-General's Department, in conjunction with the new Small Business and Family Enterprise Ombudsman and the ACCC, to monitor and collect evidence of unfair contract terms in MI Act contracts. If appropriate, the treatment of marine insurance contracts could be revisited.

Furthermore, the General Insurance Code of Practice (the Code) also applies to many marine insurance contracts. The Code sets out the standards that general insurers must meet when providing services to their customers, such as being open, fair and honest. It also sets out timeframes for insurers to respond to claims, complaints and requests for information from customers.

As most combined cargo policies written by the Australian marine insurance market provide that either the MI Act or IC Act may apply (as outlined above), many marine insurance combined cargo policy wordings include specific reference to the Code – those insurers accept that the principles of the Code apply.

The Code covers many aspects of a customer's relationship with their insurer, from buying insurance to making a claim, to providing options to those experiencing financial hardship, to the process for those who wish to make a complaint.

There would be no detriment to small business from an exemption

The proposed exemption would avoid potential uncertainty and confusion for small business and ensure that their existing rights and obligations under the MI Act are not compromised. The Insurance Council reiterates that there has been no experience of customers – small businesses or otherwise – contesting MI Act contracts due to unfair contracts terms.

The Insurance Council submits that the proposed exemption would have a neutral effect on small business compliance costs. Small business' long-established rights and obligations under the MI Act would remain unchanged. Conversely, extending the Small Business UCT Law to MI Act insurance contracts would impose on small businesses an unnecessary layer of regulatory complexity. This would require small businesses to allocate already scarce resources to try and comprehend a level of protection that is already provided for under the MI Act. This would have a real negative effect on small business productivity and impede the sector's ability to grow and contribute to the national economy.

The Insurance Council notes that Australian marine insurance providers have a duty under section 23 of the MI Act to ensure that all insureds – including small business policy holders – are aware of their rights and obligations under the MI Act. As pointed out by the ALRC[5], this includes where an insurer has made representations about the effect of clauses restricting the ambit of the policy; where there are unusual clauses which have not been

[5] Australian Law Reform Commission 2001, *Review of the Marine Insurance Act 1909*, ALRC Report 91, pages 190-191.

brought to the attention of the insured; in making determinations about particular matters under the contract of insurance; and in dealing with and settling claims.

The role of insurance intermediaries

The Insurance Council appreciates that the Small Business UCT Law is intended to support small businesses that are unable due to limited time, expertise, and bargaining power to avoid potentially unfair contract terms when negotiating with an insurer.

However, commercial marine insurance contracts – including for small business – are not directly negotiated between an insured and insurer. Rather, these contracts are negotiated through insurance intermediaries (i.e. an insurance broker) that act on behalf of their purchasing clients and represent their client's best interests. Notably, the intermediary's client does not interact with the insurer during contract negotiations.

Intermediaries provide advice in the interests of their clients, helping their clients identify their individual and/or business risks to help them decide what to insure, and how to manage those risks in other ways. Intermediaries are aware of the terms and conditions, benefits and exclusions and costs of a wide range of competing insurance policies, so they can help their clients find the most appropriate cover for their own circumstances.

Indeed, intermediaries would also be able to provide advice to clients on any potential unfair contract terms and significantly, have considerable bargaining power to negotiate favourable terms on behalf of their insureds, due to their buying power and their ability to do business with different insurers. This levels the playing field, negating the need for the protections under the Small Business UCT Law.

In addition, insurance intermediaries also have a duty – under section 25 of the MI Act – to ensure that insureds are aware of their rights and obligations. The proposed exemption would not diminish those duties.

Given the relationship between the consumer, intermediary and insurer, the Insurance Council submits that it is unnecessary to extend the Small Business UCT Law to contracts under the MI Act, as the proposed protections are intended to specifically target direct end consumer-insurer relationships.

The proposed exemption is not contrary to the public interest

In looking at the effect of the proposed exemption on the public interest, it is important to carefully evaluate the economy-wide implications. The Insurance Council has considered this matter carefully and submits that the proposed exemption would not be contrary to the public interest.

Reflecting the global nature of marine law, marine insurance providers around the world – including in Australia – operate in what is a highly competitive international market. This has enabled Australian small businesses to make selective choices about their marine insurance needs from competitive domestic providers. Therefore, it is in the best interests of all Australian stakeholders that the Small Business UCT Law does not interfere with contracts under the MI Act.

The proposed exemption would help ensure that small business' access to Australian marine insurance products is supported through the safeguarding of Australian marine insurance

providers' international competitiveness. As outlined above, an exemption would also help safeguard the sustainability of associated domestic industries including surveyors, other service providers appointed by insurers and local dispute resolution and litigation services.

Should the Small Business UCT Law be extended to MI Act contracts, the ensuing uncertainty is likely to result in higher premiums or reinsurance charges for Australian insurers and/or insurers becoming more selective. This may force domestic providers to exit the market and severely disrupt the supply of Australian marine insurance products and associated services. Ultimately, the effect of this on consumer welfare would be detrimental.

The proposed exemption would not alter the behaviour of Australian marine insurers or their intermediaries. It would allow insurers to continue to offer Australian small businesses competitive marine insurance products that are consistent with long-established and well-understood international practices. Australian marine insurance providers and their intermediaries have always worked to ensure that their customers are fully aware of their rights and obligations under the MI Act – the proposed exemption would not change this.

The Insurance Council has carefully considered whether any other community groups might be affected by the proposed exemption. However, we are unaware of any other community groups that may be affected.

Based on these arguments, the Insurance Council submits that the proposed exemption would not be contrary to the public interest, given the material benefits that an exemption would provide to Australian consumers, small businesses, marine insurance providers and associated industries.

Developments in the United Kingdom

The United Kingdom's (UK) Consumer Rights Act (CR Act) came into force on 1 October 2015. Parts 1 and 2 of the CR Act consolidate and replace the UK's former Unfair Terms in Consumer Contracts Regulations (UTCCRs) and relevant provisions of its Unfair Contract Terms Act[6] (UCTA).

We understand that the unfair contract term protections under the UK's CR Act apply to marine insurance, so far as the contracting party is a 'consumer'[7]. We also understand that the extension of the term 'consumer' to include small business was considered but not adopted. Therefore, the new UK legislation does not appear to apply to marine insurance contracts with small business.

In the UK, protection for small business from unfair contract terms in marine insurance contracts is provided for under Section 17 of the UK's *Marine Insurance Act 1906*, which provides that marine insurance contracts are contracts 'based upon the utmost good faith'. As pointed out earlier, the UK legislation is the basis of current marine law in Australia and many of Australia's major trading partners.

---

[6] Guidance on the unfair terms provisions in the United Kingdom's Consumer Rights Act states that the UCTA will be amended so that it covers business to business and consumer to consumer contracts only.

[7] The United Kingdom's CR Act defines a consumer as "… *an individual acting for purposes that are wholly or mainly outside that individual's trade, business, craft or profession*". The requirement that the consumer be an individual excludes companies from claiming consumer rights under the CR Act.