Mr Aidan Storer
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9 December 2016

Dear Mr Storer

AUSTRALIAN CONSUMER LAW REVIEW INTERIM REPORT

The Insurance Council of Australia[1] (Insurance Council) appreciates the opportunity to provide its views on the *Australian Consumer Law Review Interim Report* (the Interim Report). We understand that the Final Report will be presented to the Legislative and Governance Forum on Consumer Affairs in March 2017.

The chief purpose of this submission is to reaffirm the Insurance Council's position that consumers have strong protections under the existing comprehensive regulatory regime applying to insurance and that there is no need for contracts covered by the *Insurance Contracts Act 1984* (IC Act) to also be subject to similar protections against unfair contract terms (UCT) as under the Australian Consumer Law (ACL) and *Australian Securities and Investments Commission Act 2001* (ASIC Act).

The submission also provides our views on other suggestions raised in the Interim Report, including whether 'contracts as a whole' should be declared void under certain circumstances and the ASIC Act should cover financial products as well as services.

Unfair Contract Terms & Insurance Contracts

Strong protections are already in place

As explained in our May 2016 submission[2] to the *Australian Consumer Law Review Issues Paper*, the Insurance Council considers that the existing regulatory regime already provides a high level of protection to consumers from UCT in relation to general insurance they

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[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 2016 Australian Prudential Regulation Authority statistics show that the private sector insurance industry generates gross written premium of $44.1 billion per annum and has total assets of $120.5 billion. The industry employs approximately 60,000 people and on average pays out about $124.6 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).

[2] Insurance Council of Australia's 27 May 2016 submission to the Australian Consumer Law Review Issues Paper refers.

purchase. Therefore, the UCT provisions under the ACL and ASIC Act need not be extended to insurance contracts regulated under the IC Act.

We emphasised that the IC Act places an obligation on insurers and insureds to act with utmost good faith towards each other, preventing either party from relying on a contract provision that would be contrary to this requirement. The IC Act's preamble describes its broad intent as:

> "*An Act to reform and modernise the law relating to certain contracts of insurance so that a **fair** balance is struck between the interests of insurers, insureds and other members of the public and so that the provisions included in such contracts, and practices of insurers in relation to such contracts, operate **fairly**, and for related purposes*." (Our emphasis).

The Attachment explains how the IC Act already provides a UCT regime designed for insurance.

We also highlighted the benefit of additional protections available to insurance policy holders under the *Corporations Act 2001*, the external dispute resolution mechanism provided by the Financial Ombudsman Service and the General Insurance Code of Practice.

Further to this, we noted that financial services product issuers and distributors will soon be subject to additional obligations – as recommended by the Financial System Inquiry and accepted by the Government – to ensure that product design and distribution processes result in appropriate consumer outcomes. ASIC will also be given product intervention powers that will substantially enhance its regulatory toolkit.

On this basis, we continue to submit that these protective measures provide equivalent, if not greater, protections to consumers from UCT in relation to insurance they purchase, relative to the UCT provisions under the ACL and ASIC Act.

Absence of evidence indicating unfairness

The Insurance Council considers that any deliberation on extending the UCT provisions to IC Act contracts should only be undertaken in light of clear evidence that existing remedies fail to address imbalances in negotiating power, or where consumers are currently experiencing disadvantage or loss as a result of unfair contract terms.

We do not believe that evidence has been presented – in the Interim Report or otherwise – to suggest that there is unfairness in insurance contracts for which remedies do not exist. Indeed, if this were the case, there would be a much higher number of complaints. With respect to the examples of possible unfair terms raised by some stakeholders in the Interim Report[3], we do not consider that they demonstrate a need for the UCT provisions to apply to insurance contracts.

The Financial Ombudsman Service (FOS) for instance, in relation to the first two examples cited, would be able to adjudicate a settlement that was fair in all the circumstances. Depending on the specific circumstances of the case, an insurer trying to rely upon the provisions in question could well be in breach of the duty of utmost good faith within the IC

[3] Box 19, page 122 of the Australian Consumer Law Review Interim Report.

Act. That is, to act without regard to community and commercial standards of decency, fairness and fair dealing and without due regard to the interests of the other party.

Importantly, amendments made to the IC Act in 2013 significantly strengthened the protections available to insureds with respect to potential breaches of the duty of utmost good faith. Critically, a breach of the duty of utmost good faith would be a breach of section 13(2) of the IC Act. This would enable ASIC to pursue action against an insurer under the *Corporations Act 2001. U*nder the provisions of this Act, ASIC has the power to, among other enforcement actions, suspend or cancel an insurer's Australian Financial Services Licence (Subdivision C of Division 4 of Part 7.6).

However, the Insurance Council is unaware of ASIC attempting to exercise its additional powers under the IC Act for any breach (or breaches) of the duty of utmost good faith. This presumably would have occurred if consumers were being treated unfairly to the extent alleged by some stakeholders. The Insurance Council believes that time should be given for ASIC to apply its new powers against any perceived problems before any further legislative change is considered.

In relation to the third example, the *Disability Discrimination Act 1992* (Cth) and other anti-discrimination laws offer existing comprehensive remedy.

The Interim Report also cited the Australian Government's November 2012 estimate[4] – based on FOS claims and dispute data – that 75 to 150 consumers per year suffer disadvantage as a result of UCT in general insurance. However, we believe it is important to clarify that the Australian Government qualified its analysis as being a "rough" estimate, and added that the estimated level of consumer detriment would be "insignificant" in aggregate:

> "*In considering the available information on the number of claims affected by UCT, a* ***rough estimate*** *suggests there* ***may be*** *75-150 consumers per year suffering disadvantage as a result of UCT in insurance … Regarding the size of detriment caused by UCT, the limited available evidence suggests consumer detriment … is* ***unlikely to be significant in aggregate***." (Our emphasis).

In determining whether there is unaddressed unfairness in insurance contracts, it is also important to consider any potential estimate in the context of the total number of general insurance policies that are purchased by millions of Australian consumers every year.

The General Insurance Code Governance Committee's 2014-15 General Insurance Industry Data Report[5] shows that the general insurance industry issued or renewed around 52 million general insurance policies in the year to 30 June 2015. The large majority of these were personal insurance policies (around 48 million) in the motor, travel and home classes – collectively, these accounted for more than three quarters of all personal insurance policies.

Out of the total number of policies, consumers and businesses lodged around 4 million general insurance claims. Of these claims, 97 per cent were paid (the claims paid percentage has been broadly consistent for a number of years). The Australian Government

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[4] Australian Government, Regulation Impact Statement: Unfair Terms in Insurance Contracts November 2012, page 19.

[5] General Insurance Code Governance Committee: *The General Insurance Industry Data Report 2014-2015, 2012 General Insurance Code of Practice*, pages 7, 15 and 31. Released 2 June 2016. The 2015-16 edition is scheduled for release in 2017.

has acknowledged that "*general insurance claims data show that only a small fraction of claims are denied*" [6].

Of the 3 per cent of claims that were not paid, a small proportion of these resulted in internal disputes received by general insurers (23,105). The vast majority of these disputes (98 per cent) were handled by general insurers' own Internal Dispute Resolution processes.

Therefore, the number of internal disputes received by general insurers, represented as a proportion of the total number of general insurance policies issued or renewed in 2014-15, was 0.04 per cent (about 4 disputes received for every 10,000 policies issued or renewed). Furthermore, the number of disputes which went on to be accepted for resolution by FOS in 2014-2015 was 6,780 (or 0.01 per cent of the total number of general insurance policies issued or renewed that year).

The Interim Report also cited the Productivity Commission's (the Commission) 2008 Review of the Australian Consumer Policy Framework[7] as supporting a regulatory approach that would address unfair contract terms economy-wide.

The Insurance Council believes it should be clarified that the Commission took a whole-of-economy approach to considering UCT laws, with no specific consideration given to UCT laws in the insurance context. Also, the Commission identified the following concerns regarding disclosure that we strongly submit the UCT provisions would not solve:

- Many disclosure documents for standard goods and services meet the legal requirement for disclosure, but may not be read by consumers. Consumers are therefore unlikely to be aware of detailed terms and conditions of contractual arrangements.
- Contracts are often lengthy and difficult to understand, and consumers often have limited time to read and fully comprehend the contract.

The Insurance Council is currently undertaking a large scale research project to facilitate more effective disclosure outcomes.

Potential implications of extending UCT provisions to insurance contracts

The Insurance Council submits that extending the UCT provisions to insurance contracts could potentially result in a number of significant negative implications for consumers and general insurers.

In particular, the resulting uncertainty as to whether a term necessary to limit the insurer's risk could be found void may lead to increases in the cost of insurance and therefore higher premiums and/or the withdrawal of cover by insurers in risky market segments, which may diminish competition in those segments.

Insurance policies are priced according to the scope of cover provided and the likelihood and cost of possible claims. General insurers use terms in policies – such as exclusions – as a tool to define risk and determine premium pricing. The unnecessary layering of the UCT provisions upon the existing remedies may result in the voiding of terms, including terms that define the scope of cover.

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[6] Australian Government, Regulation Impact Statement: Unfair Terms in Insurance Contracts November 2012, page 18.

[7] Productivity Commission, *Review of Australia's Consumer Policy Framework Inquiry Report*. Released 8 May 2008.

Furthermore, extending the UCT provisions to insurance contracts may also affect the availability of reinsurance (typically provided by large specialist insurance companies with well-diversified global operations). A reinsurer will specify what they will and will not cover and an insurer will define the extent of cover it can offer consumers accordingly. Should a term commonly used within an insurance contract be found to be void as an UCT this could have significant consequences for an insurer's reinsurance protection, as it may leave the insurer exposed to the full extent of the claims.

Previous Insurance Council submissions have explained that is impossible to predict the legal impact of applying UCT protections to insurance contracts. On some views, exclusion clauses would not be generally open to review because they define the subject matter of the contract. Other authorities hold that the subject matter of an insurance contract may be taken by the Courts to be limited to whether the contract provides for example, cover for a motor vehicle or home contents. The impact on insurers therefore may vary from at a minimum having to review their contracts and manage uncertainty to having business models overturned and risks imposed on them which they had never envisaged accepting.

Given that the existing protections are effective and the lack of compelling evidence of unfairness in insurance contracts, the Insurance Council strongly recommends that the Government does not extend the UCT provisions to insurance contracts regulated under the IC Act.

The need for careful consideration

The Insurance Council submits that if the ACL Review concludes that insurance contracts should be subject to UCT provisions, then for all the reasons put above explaining the complexity of insurance regulation, the Insurance Council would urge the need for an insurance specific remedy to be developed for insertion into the IC Act.

Other Issues

Contracts as a whole

This Insurance Council notes that the Interim Report canvasses suggestions by some stakeholders that contracts as a whole should be declared void if they, for example, lack accessibility, transparency, or because they offer such 'poor value' they could in their entirety be considered unfair. However, we consider that this would be unnecessary given the adequacy of the existing protections that apply to contracts more generally.

As noted in the Interim Report, the ACL already provides for terms to be construed in the context of the contract as a whole; this is bolstered by other protections against unconscionable conduct, misleading or deceptive conduct, and false or misleading representations, and the cooling-off period for unsolicited consumer agreements.

Additionally, this suggestion would jeopardise more consumers than it would benefit, particularly if one standard contract that was issued to potentially thousands of customers was unnecessarily void without warning.

ASIC Act coverage

The Interim Report seeks views on a suggestion that the ASIC Act should be amended to

explicitly apply various consumer protections[8] (e.g. regarding misleading and deceptive conduct) to financial products as well as services.

The Insurance Council submits that this would be unnecessary, principally as the coverage of the term 'financial services' within the ASIC Act is broad and in effect adequately captures financial products as well.

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

[8] Page 33 of the Australian Consumer Law Review Interim Report: misleading or deceptive conduct; false or misleading representations; offering rebates, gifts, prizes, etc.; certain misleading conduct in relation to financial services; bait advertising; referral selling; accepting payment without intending or being able to supply; and harassment and coercion.

INSURANCE COUNCIL OF AUSTRALIA

ATTACHMENT

HOW THE IC ACT ALREADY PROVIDES A UCT REGIME DESIGNED FOR INSURANCE

The law applying to insurance contracts provides comprehensive protections to Australian consumers. In particular section 14 of the IC Act arguably operates more widely, more fairly and more powerfully than the UCT provisions currently applied to contracts other than contracts of insurance. Section 14 of the IC Act states:

> **"*14 Parties not to rely on provisions except in the utmost good faith***
>
> *(1) If reliance by a party to a contract of insurance on a provision of the contract would be to fail to act with the utmost good faith, the party may not rely on the provision.*
>
> *(2) Subsection (1) does not limit the operation of section 13.*
>
> (3) *In deciding whether reliance by an insurer on a provision of the contract of insurance would be to fail to act with the utmost good faith, the court shall have regard to any notification of the provision that was given to the insured, whether a notification of a kind mentioned in section 37 or otherwise.*"

Utmost good faith is not defined in the IC Act. It is a flexible concept which addresses unfairness according to the circumstances. There are a number of judicial descriptions of the duty of utmost good faith. The most authoritative are to be found in the judgment of the High Court in *CGU Insurance Ltd v AMP Financial Planning Pty Ltd* (2007) 235 CLR 1. In that case, their Honours Gleeson CJ and Crennan J described an insurer's utmost good faith in terms which have become widely accepted. They stated (at [15]):

> "… *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*."

This 'insurance UCT regime' is wider and operates more fairly than any other UCT regime. The following matters, in particular, show this:

(a) As stated above, terms in an insurance contract cannot be relied upon if to do so would be to fail to act with utmost good faith. That is, if to do so would be to act other than according to commercial standards of decency and fairness, without due regard to the interests of the insured;

(b) The 'insurance UCT regime', like the UCT provisions is not confined to terms that are always unfair. Rather, terms that operate unfairly, be it for a particular customer or for every customer, are caught by section 14 and would also be subject to section 13, which is addressed below;

(c) The 'insurance UCT regime' applies to all terms of a contract of insurance. There is no carve-out for certain terms such as terms that define the main subject-matter of the contract (invariably excepted from other UCT regimes).

(d) Much has been said about the difficulty of applying a subject-matter exception to contracts of insurance;

(e) The ‘insurance UCT regime’ governs all contracts of insurance and is not restricted to consumer contracts. It applies equally to an individual as it does to a business with thousands of employees; and

(f) The remedy under section 14 of the IC Act is that an insurer may not rely upon a term if to do so would be to act contrary to its duty of utmost good faith. If a Tribunal finds that an insurer will be in breach of its duty of utmost good faith because a term is inherently unfair then any further reliance is likely to a breach of section 13 of the IC Act which invokes the powers of ASIC under that section.