NATIONAL INSURANCE BROKERS ASSOCIATION OF AUSTRALIA (NIBA)

SUBMISSION ON UNFAIR TERMS IN INSURANCE CONTRACTS

DRAFT REGULATION IMPACT STATEMENT FOR CONSULTATION

24 February 2012

ABOUT NIBA

NIBA is the voice of the insurance broking industry in Australia. NIBA represents 500 member firms and over 2000 individual Qualified Practising Insurance Brokers (QPIBS) throughout Australia.

Brokers handle almost 90% of the commercial insurance transacted in Australia, and play a major role in insurance distribution, handling an estimated $16 billion in premiums annually and placing around half of Australia's total insurance business. Insurance brokers also place substantial insurance business into overseas markets for large and special risks.

Over a number of years NIBA has been a driving force for change in the Australian insurance broking industry. It has supported financial services reforms, encouraged higher educational standards for insurance brokers and introduced a strong independently administered and monitored code of practice for members. The 500 member firms all hold an Australian financial services (AFS) licence under the Corporations Act that enables them to deal in or advise on Risk Insurance products.

ABOUT INSURANCE BROKERS

The role of insurance brokers

The traditional role of insurance brokers is to:

- assist customers to assess and manage their risks, and provide advice on what insurance is appropriate for the customer's needs;
- assist customers to arrange and acquire insurance; and
- assist the customer in relation to any claim that may be made by them under the insurance.

In doing the above the insurance broker acts on behalf of the customer as their agent. Insurance brokers offer many benefits to customers and consumers:

- assistance with selecting and arranging appropriate, tailored insurance policies and packages
- detailed technical expertise including knowledge of prices, terms and conditions, benefits and pitfalls of the wide range of insurance policies on the market;

- assistance in interpreting, arranging and completing insurance documentation;
- experience in predicting, managing and reducing risks; and
- assistance with claims and a higher success rate with settlements (about 10 per cent higher than claims made without a broker).

In limited cases insurance brokers may act as agent of the insurer not the insured but where such a relationship exists the customer is clearly advised up front.

EXECUTIVE SUMMARY

NIBA is pleased to be able to make a submission to on the Draft Regulation Impact Statement (RIS).

NIBA supports any change that appropriately addresses any imbalance between protections offered under the existing regulation of insurance contracts and that which currently applies to other financial products and services, which may result in actual or potential disadvantage or loss to consumers due to insurance contracts containing terms that are harsh and/or unfair.

NIBA strongly agrees with the Productivity Commission commentary1 that "Regulation provides key foundations for a well-functioning economy. But regulation generally comes with costs as well as benefits for society."2

Given the nature of insurance contracts and the fact that specific legislation was enacted to deal with the unique issues associated with them it is crucial that before any reform is implemented proper consideration be given to whether the principles of good regulation have been met.

Based on the information provided in the RIS, NIBA is concerned that it is not clear that the changes proposed:

- are justified on any sound legal and empirical basis;
- will produce benefits that justify costs, considering the distribution of effects across society and taking economic, environmental and social effects into account;
- will minimise costs and market distortions; and
- will promote innovation through market incentives and goal-based approaches3.

NIBA is however open to considering changes to the Insurance Contracts Act if it can be established that there is a significant gap in protection and the costs of making the change to consumers,

1 This discussion is taken from commentary in the Productivity Commission Research Report Identifying and Evaluating Regulation Reforms, December 2011

2 Productivity Commission 2011, page 9

3 Productivity Commission 2011, page 10

insurers and insurance brokers do not outweigh the benefits. At present it is not obvious to NIBA that this is the case.

For this reason, NIBA is only able to support the status quo option.

To the extent that change is to be made based on the information available in the RIS, NIBA believes the most appropriate model would be Option B with:

- changes being included in the Insurance Contracts Act 1984 (Cth) (**IC Act**);
- reversal of the onus of proof on section 14 of the IC Act;
- Option 1 - main subject matter is broadly defined to include limitations or exclusions that impact on the scope of insurance cover with consumer having the right to seek blanket avoidance ie not limited to Regulator.

NIBA believes that where changes are made, a comprehensive Post Implementation Review should be conducted.

NIBA sets out below its view regarding the principles of sound regulation followed by a response to each of the Consultation Questions.

PRINCIPLES OF SOUND REGULATION

NIBA strongly agrees with the Productivity Commission commentary4 that "Regulation provides key foundations for a well-functioning economy. But regulation generally comes with costs as well as benefits for society."5

The Productivity Commission cites the Organisation for Economic Cooperation and Development's observation that "good" regulation should:

- Serve clearly identified policy goals, and be effective in achieving those goals
- Have a sound legal and empirical basis
- Produce benefits that justify costs, considering the distribution of effects across society and taking economic, environmental and social effects into account
- Minimise costs and market distortions
- Promote innovation through market incentives and goal-based approaches
- Be clear, simple, and practical for users
- Be consistent with other regulations and policies

4 This discussion is taken from commentary in the Productivity Commission Research Report Identifying and Evaluating Regulation Reforms, December 2011

5 Productivity Commission 2011, page 9

- Be compatible as far as possible with competition, trade and investment-facilitating principles at domestic and international levels6.

Australian Governments have agreed that these principles are appropriate for this country, and have expressed this agreement in the COAG National Partnership Agreement to Deliver a Seamless National Economy.

Unfortunately, not all regulation complies with these core principles. In 2006 the Federal Government Regulation Taskforce identified five features of regulations that contribute to compliance burdens on business that are not justified by the intent of the regulation.

They are:

- Excessive coverage, including 'regulatory creep' – regulations that appear to influence more activity than originally intended or warranted, overly prescriptive, or where the reach of regulation impacting on business, including smaller businesses, has become more extensive over time.
- Regulation that is redundant – regulations that have become ineffective or unnecessary as circumstances have changed over time.
- Excessive reporting or recording requirements – multiple demands from different areas of government for similar information.
- Variation in definitions and reporting requirements –these variations can generate confusion and extra work for businesses than would otherwise be the case.
- Inconsistent and overlapping regulatory requirements – regulatory requirements that are inconsistently applied, or overlap with other requirements, either within governments or across jurisdictions.7

The Productivity Commission also notes the policy of the Australian Government to develop and publish a Regulatory Impact Statement for any new proposed regulation. This is important, because regulation can impose costs on the Government and on businesses directly affected by the regulations, and can also result in economic distortions and benefits being forgone through unintended consequences and other perverse effects8.

Where a comprehensive Regulatory Impact Statement has not been prepared or is not sufficiently comprehensive, Australian Government policy requires a Post Implementation Review, which is to be undertaken within one to two years of the regulations being implemented.

6 Productivity Commission 2011, page 10

7 Productivity Commission 2011, page xiv

8 For discussion of the need to properly assess the benefits and costs of regulation, see Productivity

WHY INSURANCE IS DIFFERENT

The fundamental and long standing doctrine governing insurance contracts is that of "utmost good faith" (the doctrine of *uberrimae fides*). Both the buyer and the seller of an insurance product must make a full declaration of all material facts at the outset, before the contract is entered into. This principle is of long standing in the common law (case law) of insurance, and has been embedded in the insurance law of Australia by means of section 13 of the *Insurance Contracts Act 1984* (Cwlth.).

In addition to the doctrine of utmost good faith, insurance contracts are regulated extensively through the *Insurance Contracts Act*, which was enacted following an extremely thorough review of insurance contract law by the Australian Law Reform Commission and a more recent review in 2003/4 in which only minor changes were recommended. These were ultimately included in the Insurance Contracts Amendment Bill 2010 (Cth) which has not proceeded. These changes are expected to be finalised this year in new draft legislation.

Provisions of the *Insurance Act* and Chapter 7 of the *Corporations Act* are also relevant in relation to the operation of insurance policies, and the rights and obligations of parties under those policies.

By contrast, most typical market activity is subject to the principle of "let the buyer beware" (otherwise known as *caveat emptor*). General provisions such as those in the Australian Consumer Law have been developed over time to protect purchasers of goods and services from unfair and unscrupulous market conduct.

Finally, it is important to note that under an insurance policy, the purchaser does not receive a tangible (physical) product or service. In return for the agreed premium, the policyholder receives an undertaking or a promise from the insurer. The promise only comes into effect an insured event occurs, and the policyholder has suffered a loss covered by the policy. In the great majority of insurance policies, the policyholder receives the benefit of the protection afforded by the policy, but does not receive anything further unless or until an insured event occurs.

CHAPTER 2 THE PROBLEM

Consultation Question 1

A. In practical terms, is the current consumer protection provided in relation to the use of unfair terms in the Insurance Contract Act 1984 adequate?

As the RIS notes, the current Insurance Contracts Act provisions and other relevant law do not cover the same breadth of circumstances as the unfair contract terms provisions.

NIBA supports the imposition of similar standards on insurance contracts as those under the unfair contracts provisions, provided such changes are justified on sound regulatory principles as discussed above.

NIBA is concerned that it is not clear that the changes proposed:

- are justified on any sound legal and empirical basis;
- will produce benefits that justify costs, considering the distribution of effects across society and taking economic, environmental and social effects into account;
- will minimise costs and market distortions; and
- will promote innovation through market incentives and goal-based approaches .

NIBA's view is that the protection provided by the Insurance Contracts Act for consumers relevant to unfair terms, whilst not identical to the unfair contracts provisions, is what it would consider to be a relatively high standard.

In addition, the provisions of the Corporations Act 2001 (Cth) (the Corporations Act), the free (to consumers) external dispute resolution scheme provided by the Financial Ombudsman Service (FOS) and the General Insurance Code of Practice (the Code) all add to this protection.

The effect of the relevant provisions in the Insurance Contracts Act is that an insurer will not be able to rely on a term in an insurance contract if reliance on that term can be seen to be in breach of its duty to act with the utmost good faith. It will be determined on a case by case basis.

Conduct by the insurer that amounts to unfair dealing will be seen as being in breach of the insurer's duty to act with the utmost good faith.

ASIC can similarly, under s55A of the Insurance Contracts Act, bring an action if it is satisfied that insureds have suffered damage, or are likely to suffer damage, because of the terms of the contracts or the conduct of the insurer breaches the provisions of the Insurance Contracts Act.

This power will be extended to s13 breaches under the proposed changes to the Insurance Contracts Act. ASIC will also be able to bring an action under the Corporations Act in relation to such a breach pursuant to an insurers Australian Financial Services Licence conditions , including in relation to claims handling and settlement.

NIBA is of the view that the relevant provisions in the Insurance Contracts Act provide similar but not identical protection to consumers against terms which might be unfair in insurance contracts.

In order to establish that a term is unfair, and therefore void, it needs to be proven that the term:

- would cause a significant imbalance in the parties' rights and obligations under the standard form contract; and
- is not reasonably necessary to protect the legitimate interests of the party who would be advantaged by the term.

The onus of proof will lie on the claimant (usually the consumer or ASIC) to establish that the term in a standard form contract has caused a significant imbalance in the parties' rights and obligations under the standard form contract. This needs to be proved on the balance of probabilities. S3(4) provides that unless the defendant (usually the business) can prove otherwise, there is a presumption that the term is not reasonably necessary to protect the legitimate interests of the party who would be advantaged by the term.

There is also a rebuttable presumption that the contract is a standard form contract and the onus is on the business to prove otherwise. If a party wishes to argue that the contract has been negotiated and is not in a standard form, then the party is required to present the contract to show that the contract is not a standard form contract.

Under the Insurance Contracts Act the onus of proof is also on the claimant to establish that the other party did not act with the utmost good faith when relying on a term in the insurance contract.

Accordingly, under the both systems the onus of proof will remain on the claimant to establish that the term has caused a significant imbalance in the parties' rights and obligations.

The main difference is that under the generic provision the business party will bear the onus to rebut the presumptions that the contract is a standard form contract which is simply a trigger for the legislation's applicability. There is no such restriction in the Insurance Contracts Act and such a restriction would appear difficult to incorporate sensibly in the context of the Act's other provisions.

There are a number of other provisions in the Insurance Contracts Act that ensure insurance companies cannot take advantage of uniformed consumers.

These provisions provide specific remedies for the insured that are appropriate for insurance transactions and do not simply void the provisions as would occur under the generic provision in the ASIC Act.

Relevant provisions in the Insurance Contracts Act include;

- Avoiding a contract for fraud (s31).
- Minimum claim amounts in relation to certain types of insurance (s35 see table above).
- Requirement that pre-contractual written notice be provided of unusual terms (s37 see table above).
- Rendering void provisions in interim contracts of insurance that make the application to, or the acceptance of replacement cover by the insurer a condition precedent to the interim cover (s38).
- Excluding or limiting liability due to another insurance contract (s45).
- Relying on exclusions regarding pre-existing defects, imperfections and pre-existing sickness or disability (ss 46 and 47).
- Termination of some renewable insurance contracts (section 58).

Specific insurance industry solutions offer insurance consumers a far higher level of protection than the generic provision under the ASIC Act.

Because the duty of utmost good faith is an implied term in every contract of insurance, the insured will be able to claim any contractual remedies. This will include seeking remedies under the Insurance Contracts Act.

Under both the ASIC Act and the Insurance Contracts Act, ASIC has the right to bring actions on behalf of consumers (insureds in the case of the Insurance Contracts Act), when ASIC is satisfied that the consumer has suffered damage, or is likely to suffer damages as a result of a term in a contract to which the consumer is a party.
The ASIC Act also provides the consumer with the right to obtain an injunction against the business party to the standard form contract.

Under the current arrangements ASIC has a similar right to obtain an injunction against insurers for a breach by the insurer of the provisions of s12 of the ASIC Act.

Part IA of the Insurance Contracts Act gives ASIC responsibility for the general administration of the Insurance Contracts Act and vests in ASIC a number of specific powers to support this role, such as the power to obtain documents.

A new section 11F is likely to be inserted into the Insurance Contracts Act that gives ASIC powers to intervene in matters arising under the Act. The provision is similar in form to the existing power that ASIC has to intervene in proceedings begun by other persons about matters arising under the Corporations Act 2001 (section 1330). It allows ASIC to be represented in the proceedings by a staff member, a delegate, a solicitor or counsel.

An insured who is a party to an insurance contract has the additional remedy of lodging a dispute with the Financial Ombudsman Service. The Financial Ombudsman Service may make the following orders:

- it may decide that the insurer "undertake a course of action to resolve the dispute" including specified matters such as the payment of a sum of money, the forgiveness or variation of a debt or the meeting of a claim under an insurance contract by, for example, repairing, reinstating or replacing items of property;

- it may decide that the insurer compensate the applicant for direct financial loss or damage; and

- it may award compensation to an applicant for consequential financial loss or damage or non-financial loss (subject to certain qualifications) up to $3,000 per claim made in the dispute. No such award can be made for a dispute arising as a result of a claim on a General Insurance Policy that expressly excludes such liability.

The new General Insurance Code of Practice also highlights the duty of utmost good faith (see clauses 1.19 and 1.20) and provides additional protection to members of the Code. NIBA notes that the Financial Ombudsman Service will also consider the Code in its decisions.

Remedies are also available to insurance policyholders under the Corporations Act.

S912A(1) - sets out the general obligations on a financial services licensee (including general insurers), these include the obligations to:

- do all things necessary to ensure that the financial services covered by the licence are provided efficiently and fairly; and
- comply with the financial services laws.

ASIC may, if the general insurer does not comply with its obligations under s912A of the Corporations Act make the following orders:

- banning orders (s920A);
- subject to s915I, suspension or cancellation of the insurer's license (s915C(1); or
- the imposition of conditions on the license.
  A consumer who is a retail client has the right to claim compensation from a licensee for loss or damage suffered because of breaches of certain Products Disclosure Statement obligations under the Corporations Act.

S1012B places an obligation on a financial services licensee to give a retail client a product disclosure statement if the licensee makes an offer to issue a financial product, or when the licensee issues a financial product.

S1013D sets out the main content requirements for a product disclosure statement and this includes:

- information about any significant benefits to which a holder of the product will or may become entitled, the circumstances in which and times at which those benefits will or may be provided and the way in which those benefits will or may be provided;
- information about any significant risks associated with holding the product;
- information about the cost of the product;
- information about any other significant characteristics or features of the product or of the rights, terms, conditions and obligations attaching to the product;
- information about the dispute resolution system that covers complaints by holders of the product and about how that system may be accessed; and
- information about any cooling-off regime that applies in respect of acquisitions of the product (whether the regime is provided for by a law or otherwise);
- any other statements or information required by the regulations.

S1021B(1) of the Corporations Act provides that a product disclosure statement will be defective if there is a misleading or deceptive statement in the disclosure document or statement.

General insurance policy wordings form part of the PDS and significant penalties apply for breaches of the above obligations.

Rights will also apply in relation to s13 breaches under the proposed changes to the Insurance Contracts Act, including in relation to claims handling and settlement.

Over and above such rights, a consumer who is an insured under a contract of general insurance has the right, under s1019B(1) to return the insurance product (during the cooling-off period) if the consumer is unhappy with the product.

The only benefits NIBA has identified after consideration of the relevant legislation would appear to be:

- onus of proof shift as explained above – this seems to be of limited value; and
- voidance of all provisions in like contracts – there are some serious commercial ramifications if this were to be applied.

NIBA makes the following comments on certain matters noted in the RIS related to support for change:

- Consumer representatives cite "overwhelming evidence of a problem" yet there is nothing in the RIS that allows NIBA to form the view as to whether this is accurate. [9];

- FOS determinations on the relevant issues would be a valid source in identifying whether consumers alleging an insurer's reliance on a provision would be in breach of its duty of utmost good faith term are unfairly disadvantaged or not;

- the RIS provides potential examples put forward by a consumer group of harsh or unfair contract terms that relate to the use of exclusion clauses see RIS page 8 para 2.6. None of the examples provide support for the argument one way or another;

- in relation to the protection provided by section 35 the RIS states [10]"A common view is that a large proportion of insureds do not read in detail the policy documents they receive from their insurers, so the protection offered by section 35 is not, in practice, an effective tool to ensure that consumers are informed about their cover." It is unclear to NIBA how the unfair contracts provisions would solve this issue. As the RIS notes, additional protection is also provided via the PDS requirements[11].

  The reality is that insurance policies are by their very nature complex documents and are difficult to summarise in a way that is not ultimately misleading to consumers. NIBA believes that the promotion of the availability of qualified

9 see page 7 para 2.5 RIS

10 see page 11 para 2.20

11 see page 13 para 2.25

practicing insurance brokers to advise consumers on such complex matters are a significant link in the chain of consumer protection;

- in relation to the protection provided by section 37 the same logic in the RIS for section 35 applies and NIBA's concern is the same as for section 35.

  The RIS [12]also provides "The use of section 37 may also be limited as it only applies to provisions 'not usually included in contracts of insurance that provide similar cover'. So, if an exclusion or limitation is generally used in relation to the type of cover concerned, section 37 offers no protection, even if the insured was not clearly informed of the term." NIBA notes that the RIS fails to mention that in such cases section 14 provides a remedy. As the RIS notes, additional protection is also provided via the PDS requirements[13].

- the statement that the duty of good faith protections (section 13 and 14 of the IC Act) are rarely used as a basis for relief as consumers do not understand their rights to make a claim would not appear to be solved by the unfair contracts regime. The RIS notes that use of the right under section 14 is "costly and cumbersome" and thus not used. Consideration of the FOS determinations on this would be worthwhile to determine if this view is accurate or not. Another question is why the unfair contracts provisions would be significantly less costly or cumbersome to use as a consumer still has to make the effort to bring an action in both cases, with the difference being the onus of proof.

- sections 53 and 54 provide a specific but limited form of protection for certain insurance contracts. These take into account the specific nature of insurance contracts and were drafted to take account of the industry. There are currently no significant concerns with how each are operating.

It is clear from the RIS that the consumer representative groups and insurer views are diametrically opposed.

In NIBA's view, to justify such a significant change, real evidence of a problem is necessary given the potential adverse impact on consumers and the industry. If there is real evidence of such a significant problem, NIBA would support any changes to better protect consumers.

12 see page 12 para 2.23

13 see page 13 para 2.25

Currently the view formed in the RIS to support the changes appears to be[14]:

- there is a risk of unfair terms in standard form insurance contracts causing loss or damage to policyholders and third party beneficiaries which, in some situations, could be significant; [NIBA notes that it is the "potential" risk and no evidence seems to be provided justifying this that allows a view to be formed that there is a real risk worthy of the changes proposed]

- there are existing laws that might help to prevent loss or damage to policyholders due to reliance on unfair contract terms [NIBA believes this is the case and that the protection is of a high standard and drafted to take into account the unique nature of the industry]; and

- the extent to which those laws are effective, or potentially effective, to address situations of unfair contract terms is debateable, but the existing laws:

    - do not cover the same breadth of circumstances as UCT laws;

      [NIBA agrees that this is the case. The issue is whether the unfair contract laws are appropriate in the insurance context or not]

    - are directed at providing remedies in individual cases where an objectionable term is sought to be relied upon, whereas UCT laws are directed at eliminating objectionable terms from standard form contracts;

      [NIBA agrees although is concerned that the blanket voidance provisions is inappropriate in the insurance context and if implemented could have a significantly adverse market impact]; and

    - have been identified by the Senate Economics Legislation Committee and the Natural Disaster Insurance Review as not providing adequate protection to consumers;

      [NIBA queries whether evidence of a problem justifying regulatory reform was behind such a view or simply the existence of a technical inconsistency in protection and a perceived risk;]

While generic unfair terms in standard contracts legislation may, in a few cases, give additional consumer protection to that offered under the Insurance Contracts Act, in NIBA's

14 see page 20 para 2.51

view, these relatively small benefits are far outweighed by the likely disadvantages that would arise in terms of compliance cost and potential confusion that could arise were there two regimes.

Insurance operates most effectively for consumers when there are clear contractual obligations and responsibilities that are well understood by both parties to the contract and this would not be likely to be the situation if separate unfair terms in standard contracts were to apply to insurance contracts.

B. Besides the provision of an additional legal avenue for consumers to explore if they are a party to a contract that has potentially unfair terms (if UCT provisions are introduced), are there any practical benefits for consumers?

The RIS seems to indicate that the main additional benefits are limited, assuming the proposed changes to the Insurance Contracts Act are made regarding the rights of ASIC to bring representative actions for a breach of section 14.

The other key difference is that if a term in a standard form contract is unfair and not a term covering the "main subject matter" of the contract the clause will be void in all agreements of the same type.

The term "main subject matter" is not defined and NIBA expects insurers would be very concerned that the effect of this provision would be to render void insuring clauses, exclusions and conditions that go to the basis of cover offered by the insurer. These restrictions are taken into account in calculating the premium paid by the consumer and thus to have them exposed to avoidance can substantially affect the nature of the whole transaction in question and ultimately the price to consumers.

There may also be complexities specific to insurance given insurance contracts are backed by reinsurance arrangements and the direct insurers are in many cases restricted to terms imposed on them by reinsurers. The impact of the voiding provisions would have a significant impact on the insurers and their ability to recover under the relevant reinsurance agreement. NIBA expects APRA would have some concern with this result.

NIBA notes that Recital 19 of the EC Directive 93/13/EEC on Unfair Terms in Consumer Contracts specifically carves out such provisions:

> "Whereas, for the purposes of this Directive, assessment of unfair character shall not be made of terms which describe the main subject matter of the contract nor the quality/price ratio of the goods or services supplied; whereas the main subject matter of the contract and the price/ratio may nevertheless be taken into account in assessing the fairness of terms; whereas it follows, inter alia, that in insurance

contracts, ***the terms which clearly define or circumscribe the insured risk and the insurer's liability shall not be subject to such assessment since these restrictions are taken into account in calculating the premium paid by the consumer***." [our bold italics]

C. Is there a reason for treating contracts of insurance different from other contracts relating to other financial products?

Insurance contracts can be distinguished from many other types of consumer contracts in that the contract for an insurance product and the product are, in effect, one and the same thing and that the 'main subject matter' of a contract, in this case insurance, is not subject to review under the generic legislation. See paragraph 6.6 of the RIS for an explanation of the relevant argument in this regard which NIBA agrees with.

D. Will equivalent protection in respect to unfair contract terms lead to beneficial outcomes for consumers? If possible can you outline any situations where these benefits can be clearly identified?

The effect of the provision relating to generic unfair contract terms in the ASIC Act is that the business party to the contract will not be able to rely on a term in a contract if the term is unfair. ASIC has the right to bring an action to void the unfair term from every relevant contract of the business and therefore the business will not be able to rely on that unfair term in any of its contracts of that nature.

What is interesting is how such a provision will be applied in practice when the "unfairness" of a term is determined based on the specific circumstances of the individual insured. How could this be applied across the board fairly? Only provisions that are unfair irrespective of the circumstances of the insured or where it will clearly apply in all circumstances would seem to be able to be fairly voided across the board.

E. **What percentage of insurance contracts and types of insurance contracts are likely to be standard form contracts in accordance with section 12BK of the ASIC Act**

Most insurance policies provided to consumers will be likely to fall within the definition of standard contacts.

OPTION A – STATUS QUO

Consultation Question 2

A. Please provide details of any additional costs or benefits of the status quo - if possible, please state the magnitude (either in dollars or qualitatively) of the costs and benefits?

In NIBA's view there would be no additional costs or benefits than those noted associated with the status quo.

NIBA supports the status quo model unless evidence supporting the other options is clearly identified.

OPTION B – ENHANCE EXISTING IC ACT REMEDIES

Consultation Question 3

A. Would you support changes to section 14 of the IC Act as a viable means to address the issue of unfair contract terms in insurance?

Subject to comments made above in relation to the onus of proof issues, if change is to occur, NIBA would support this change. This impacts less than the other options (excluding the status quo option).

B. Are there any other changes to section 14 that would increase consumer protection from unfair contract terms?

None NIBA can think of, other than those proposed by the RIS.

C. What are the potential benefits to consumers (both monetary and non-monetary) - if possible, please state the magnitude (either in dollars or qualitatively) of the benefits?

The benefit for consumers is that they would effectively obtain the equivalent protection of the unfair contracts regime (assuming a blanket ban change is not implemented) in a single piece of legislation (reducing confusion) without the compliance costs of insurers that the other options would cause. The compliance costs of the other options are likely to be passed to consumers for little added benefit.

If a blanket ban of terms found to breach section 14 is implemented significant issues arise as discussed in response to Question 1 above. NIBA would not support such a proposal without appropriate qualification of the "main subject matter" as discussed further below.

D. ***From an industry perspective, what would be the potential compliance costs (both monetary and non-monetary) associated with this option – if possible please provide the magnitude of the costs and a breakdown of categories?***

Assuming there is no blanket ban, it would be limited when compared to the options imposing the unfair contracts requirements.

E. ***If this option is adopted will insurers:***

(i) be likely to increase insurance premiums?

(ii) revisit some of their current contract offerings?

Assuming there is no blanket ban, the reversal of the onus of proof may cause cost increases but ultimately an insurer will always have to justify its position regarding why the insured should not be able to rely on section 14 so they should be minimal.

F. ***If this option is adopted, are there any:***

(i) additional costs or benefits?

(ii) factors that impact on the options feasibility?

(iii) practical limitations on insurers that would impede their ability to comply with the changes?

Assuming there is no blanket ban, we cannot think of any additional issues.

OPTION C – PERMIT THE UNFAIR CONTRACT TERMS PROVISIONS OF THE ASIC ACT TO APPLY TO INSURANCE CONTRACTS

Consultation Question 4

A. ***What are the potential benefits to consumers (both monetary and non-monetary) of adopting this option - if possible, please state the magnitude (either in dollars or qualitatively) of the benefits?***

Given the only change NIBA endorses is the changing of the onus of proof on section 14, the benefits are limited when weighed against the compliance costs and price impact of insurers having to implement the relevant changes.

B. ***From an industry perspective, what would be the potential compliance costs (both monetary and non-monetary) associated with this option - if possible please provide the magnitude of the costs and a breakdown of categories?***

NIBA notes the most significant issue for insurers would be the blanket voiding of unfair terms.

C. ***If this option is adopted will insurers:***

(i) be likely to increase insurance premiums?

(ii) revisit some of their contract offerings?

This is a matter for insurers to respond on but we expect this will be likely.

D. ***If this option is adopted, are there any:***

(i) additional costs or benefits?

(ii) factors that impact on the options feasibility?

(iii) practical limitations on insurers that would impede their ability to comply with the changes?

The issues and potential impact is comprehensively covered in the RIS.

OPTION D – EXTEND IC ACT REMEDIES TO INCLUDE UNFAIR CONTRACT TERMS PROVISIONS

Consultation Questions 5

A. ***If UCT laws were extended to include insurance, is it preferable for these laws to sit within the IC Act or ASIC Act?***

NIBA would prefer them to sit within the IC Act to reduce the potential for confusion and to make the legislation a one stop shop for such matters.

B. ***From an industry perspective, what would be the potential compliance costs (both monetary and non-monetary) associated with this option - if possible please provide the magnitude of the costs and a breakdown of categories?***

The compliance costs would be significant. Insurers will need to identify the impact on their businesses. Insurance brokers will need to be re trained in the new laws and the impact on a consumer's rights so they can properly represent consumers. This would be a costly process.

C. Would these costs be likely to be higher or lower than under Option C

Lower under option C assuming no blanket ban is applied.

D. What are the potential benefits to consumers (both monetary and non-monetary) - if possible, please state the magnitude (either in dollars or qualitatively) of the benefits?

Theoretically it will provide greater protection. This may come at a cost as insurers pass on compliance costs in the premium.

E. If this option is adopted will insurers:

(i) be likely to increase insurance premiums?

(ii) revisit some of their contract offerings?

The compliance costs would be significant. Insurers will need to identify the impact on their businesses but we expect premiums will be increased to cover the greater risk.

F. [G in RIS] If this option is adopted, are there any:

(i) additional costs or benefits?

(ii) factors that impact on the options feasibility?

(iii) practical limitations on insurers that would impede their ability to comply with the changes?

The blanket ban would be the main issue. See answer to question 1 above for a discussion in this regard.

OPTION E – ENCOURAGE INDUSTRY SELF-REGULATION TO PREVENT USE OF UNFAIR TERMS BY INSURERS

Consultation Question 6

A. What would be the costs and benefits to consumers (both monetary and non-monetary) - if possible, please state the magnitude (either in dollars or qualitatively) of the benefits?

NIBA supports industry self-regulation. It may assist industry develop ways of overcoming perceived consumer disadvantage without involving additional administrative costs that would be passed onto consumers through increased premiums. Self-regulation could also lead to better claims handling by insurers and an enhanced industry image.

Assuming consumers are not significantly worse off under the existing IC Act and other relevant legislation protection, which appears to be the case, this would be a mechanism whereby actual statistics could be obtained and the position monitored. If it turns out that there is an issue, legislative change could be made.

B. From an industry perspective, what would be the potential compliance costs (both monetary and non-monetary) associated with this option - if possible please provide the magnitude of the costs and a breakdown of categories?

Significantly less than Options B, C and D.

C. How do these compliance costs compare to options C and D?

NIBA expects they would be significantly less.

D. If this option is adopted will insurers:
(i) be likely to increase insurance premiums?
(ii) revisit some of their contract offerings?

We do not expect this would be the case.

E. If this option is adopted, are there any:
(i) additional costs or benefits?
(ii) factors that impact on the options feasibility?
(iii) practical limitations on insurers that would impede their ability to comply with the changes?

None NIBA can think of.

PART 2 - OPTIONS WHEN UNFAIR CONTRACT TERMS PROVISIONS APPLY TO INSURANCE CONTRACTS (OPTIONS C AND D)

OPTION 1 – SHOULD THE 'MAIN SUBJECT MATTER' OF AN INSURANCE CONTRACT BE DEFINED BROADLY?

Consultation Questions 7

A. Do you agree that main subject matter should be clarified in the context of insurance policy exclusions?

Yes for the reasons specified in the RIS.

B. ***Do you consider terms that sought to limit liability genuinely constitute main subject matter of an insurance contract?***

In insurance contracts, the terms which clearly define or circumscribe the insured risk and the insurer's liability (whether called an insuring clause, exclusion or condition) should constitute the main subject matter since these restrictions are taken into account in calculating the premium paid by the consumer.

There may also be complexities specific to insurance given insurance contracts are backed by reinsurance arrangements and the direct insurers are in many cases restricted to terms imposed on them by reinsurers. The impact of the voiding provisions would have a significant impact on the insurers and their ability to recover under the relevant reinsurance agreement. NIBA expects APRA would have some concern with this result.

C. ***From an industry perspective, what would be the potential compliance costs (both monetary and non-monetary) associated with this option - if possible please provide the magnitude of the costs and a breakdown of categories?***

This is the preferred option as the compliance costs would be significant if this option were not adopted.

D. ***What benefits are there for consumers (both monetary and non-monetary) - if possible, please state the magnitude (either in dollars or qualitatively) of these benefits?***

Assuming consumers are not significantly worse off under the existing IC Act and other relevant legislation protection, which appears to be the case, the benefits would seem limited.

E. ***If this option is adopted will insurers:***

(i) be likely to increase insurance premiums?

(ii) revisit some of their contract offerings?

We expect this option would result in a lesser increase than option 2(a).

F. ***If this option is adopted, are there any***

(i) additional costs or benefits?

(ii) factors that impact on the options feasibility?

(iii) practical limitations on insurers that would impede their ability to comply with the changes?

None we can think of.

OPTION 2(A) – SHOULD THE 'MAIN SUBJECT MATTER' OF AN INSURANCE CONTRACT BE DEFINED NARROWLY?

Consultation Questions 8

A. Are there any major obstacles (either legal or practical) preventing a narrow definition for main subject matter?

The concerns raised by insurers in the RIS seem to be the major obstacle.

B. From an industry perspective, what would be the potential compliance costs (both monetary and non-monetary) associated with this option - if possible please provide the magnitude of the costs and a breakdown of categories?

They would appear to be significant because of the insurer concerns raised.

C. What benefits are there for consumers (both monetary and non-monetary) - if possible, please state the magnitude (either in dollars or qualitatively) of the benefits?

There would be significant benefits for consumers as they could challenge all provisions of the policy.

D. If main subject matter was to be defined narrowly, what types of policy exclusions/ limitations should be excluded?

Ones affecting the scope of cover that also affect the premium would be the most significant.

E. If this option is adopted will insurers:
(i) be likely to increase insurance premiums?
(ii) revisit some of their contract offerings?

This seems likely because of the insurer concerns raised.

F. Will premium increases (if they occur) be higher if the subject matter is narrow rather than broad?

This seems likely because of the insurer concerns raised.

G. Are there any (if this option was adopted):

(i) additional costs or benefits not referred to above?

(iii) factors that impact on the feasibility of this option?

(iv) practical limitations on insurers that would impede their ability to comply with the changes?

The main issues are the insurer concerns raised in the RIS.

OPTION 2(B) –SHOULD UNFAIR CONTRACT TERMS PROVISIONS BE MODIFIED SO THAT THE REMEDIES ARE RESTRICTED TO EXERCISE BY A REGULATORY AUTHORITY

Consultation Questions 9

A. Do you consider it necessary (or desirable) to restrict remedies to be exercised solely by the regulator if UCT laws were extended to include insurance?

No. A consumer should be able to do so. A regulator right to bring an action regarding banning a term on a blanket basis

B. Will individual consumers have the same level of protection (as provided in the ACL and the ASIC Act) if the regulator is the only party that can seek remedies in relation to UCT?

NIBA does not support limiting any right solely to the Regulator.

C. From an industry perspective, what would be the potential compliance costs (both monetary and non-monetary) associated with this option - if possible please provide the magnitude of the costs and a breakdown of categories?

Lesser than under the options where consumer can bring the action.

D. If this option is adopted will insurers:

(i) be likely to increase insurance premiums?

(ii) revisit some of their contract offerings?

It is likely to result in an increase in premiums but not to the same extent where consumer can bring the action.

E. Are there any (if this option was adopted):

(i) additional costs or benefits not referred to above?

(ii) factors that impact on the feasibility of this option?

(ii) practical limitations on insurers that would impede their ability to comply with the changes?

None NIBA can think of.

F. If the subject matter is kept relatively narrow, will insurers face lower levels of uncertainty regarding the potential voiding of terms, if remedies in relation to UCT's are restricted to the regulator?

This is likely but NIBA would want insured to have the right as well.

Consultation Questions 15

If UCT provisions were applied to insurance, would a 2 year transition period be adequate for industry and consumers?

This would seem appropriate.

If you would like to discuss any aspect of this matter further do not hesitate to contact us.

Dallas Booth

Chief Executive Officer

Direct: +61 (0)2 9459 4305

Email: dbooth@niba.com.au

National Insurance Brokers' Association of Australia