



ASIC

Australian Securities & Investments Commission

CONSULTATION PAPER 245

Retail life insurance advice reforms

December 2015

About this paper

This consultation paper sets out ASIC's proposals to implement the retail life insurance industry reforms by making a legislative instrument that will set out:

- the maximum levels of upfront and ongoing commission payments to be paid to advisers; and
- the amount of upfront commissions to be repaid to life insurers under 'clawback' arrangements.

This paper also sets out the information we propose to obtain from life insurance providers (life insurers) to enable us to monitor the impact of the reforms.

We are seeking feedback on our proposals from life insurers, Australian financial services (AFS) licensees and their representatives (including authorised representatives) who are authorised to provide life insurance advice, and consumers.

About ASIC regulatory documents

In administering legislation ASIC issues the following types of regulatory documents.

Consultation papers: seek feedback from stakeholders on matters ASIC is considering, such as proposed relief or proposed regulatory guidance.

Regulatory guides: give guidance to regulated entities by:

- explaining when and how ASIC will exercise specific powers under legislation (primarily the Corporations Act)
- explaining how ASIC interprets the law
- describing the principles underlying ASIC's approach
- giving practical guidance (e.g. describing the steps of a process such as applying for a licence or giving practical examples of how regulated entities may decide to meet their obligations).

Information sheets: provide concise guidance on a specific process or compliance issue or an overview of detailed guidance.

Reports: describe ASIC compliance or relief activity or the results of a research project.

Document history

This paper was issued on 15 December 2015 and is based on the Corporations Act as at that date.

Disclaimer

The proposals, explanations and examples in this paper do not constitute legal advice. They are also at a preliminary stage only. Our conclusions and views may change as a result of the comments we receive or as other circumstances change.

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The consultation process

You are invited to comment on the proposals in this paper, which are only an indication of the approach we may take and are not our final policy.

As well as responding to the specific proposals and questions, we also ask you to describe any alternative approaches you think would achieve our objectives.

We are keen to fully understand and assess the financial and other impacts of our proposals and any alternative approaches. Therefore, we ask you to comment on:

- the likely compliance costs;
- the likely effect on competition; and
- other impacts, costs and benefits.

Where possible, we are seeking both quantitative and qualitative information.

We are also keen to hear from you on any other issues you consider important.

Your comments will help us develop our policy on the implementation of the life insurance reform proposals. In particular, any information about compliance costs, impacts on competition and other impacts, costs and benefits will be taken into account if we prepare a Regulation Impact Statement: see Section E, 'Regulatory and financial impact'.

Making a submission

You may choose to remain anonymous or use an alias when making a submission. However, if you do remain anonymous we will not be able to contact you to discuss your submission should we need to.

Please note we will not treat your submission as confidential unless you specifically request that we treat the whole or part of it (such as any personal or financial information) as confidential.

Please refer to our privacy policy at www.asic.gov.au/privacy for more information about how we handle personal information, your rights to seek access to and correct personal information, and your right to complain about breaches of privacy by ASIC.

Comments should be sent by 29 January 2016 to:

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What will happen next?

Stage 1	15 December 2015	ASIC consultation paper released
Stage 2	29 January 2016	Comments due on the consultation paper
Stage 3	April 2016	ASIC instrument released (effective from 1 July 2016) and notices issued

A Background to the proposals

Key points

Industry developed a set of reform proposals to address concerns about the quality of advice in the retail life insurance sector. These include:

- caps on commissions paid by life insurers to advisers; and
- the repayment, under certain circumstances, of those commissions (i.e. 'clawback').

Following the development of the industry reform proposals, on 3 December 2015, the Government released draft legislative amendments and explanatory material containing its proposed amendments to the *Corporations Act 2001* (Corporations Act) to remove the exemption from the conflicted remuneration provisions for life insurance advice, and to allow benefits to be paid to advisers if requirements imposed by ASIC are met.

The Government proposes to amend the Corporations Act to provide ASIC with a power to make a legislative instrument setting out:

- the maximum levels of upfront and ongoing commission payments permitted in relation to life insurance products; and
- the amount of upfront commission to be repaid to life insurers under clawback arrangements.

This consultation paper seeks feedback on the policy we propose to give effect to in the instrument. We are also seeking feedback on the type of information we propose that life insurers should report to ASIC to enable us to monitor the impact of the reforms.

Conflicted remuneration

- 1 Under the Future of Financial Advice (FOFA) reforms, conflicted remuneration was prohibited; however, advice in relation to life insurance¹ was exempt from this prohibition.

The ban on conflicted remuneration

- 2 Conflicted remuneration is any benefit given to an Australian financial services (AFS) licensee, or its representative, who provides financial product advice to retail clients that, because of the nature of the benefit or the circumstances in which it is given, could reasonably be expected to influence:

¹ In this consultation paper, we use the term 'life insurance', which we define in the same way as 'life risk insurance', as defined in s764A(1)E of the Corporations Act: see also 'Key terms' list.

- (a) the choice of financial product recommended to clients by the licensee or representative; or
 - (b) the financial product advice given to clients by the licensee or representative: s963A.
- 3 The *Corporations Act 2001* (Corporations Act) prohibits:
- (a) AFS licensees and their representatives (including authorised representatives) from accepting conflicted remuneration (s963E, 963G and 963H);
 - (b) product issuers and sellers from giving conflicted remuneration to AFS licensees and their representatives (s963K); and
 - (c) employers from giving their AFS licensee or representative employees conflicted remuneration for work they carry out as an employee (s963J).

Exemption for advice on life insurance

- 4 The Corporations Act currently provides for certain circumstances in which the benefits given to an AFS licensee or its representatives are not conflicted remuneration, including if the benefits are given in relation to advice on life insurance products: s963B(1)(b). The FOFA reforms did not extend the ban on conflicted remuneration to individual life insurance sales.
- 5 However, the Parliamentary Joint Committee on Corporations and Financial Services, in its inquiry into the Corporations Amendment (Future of Financial Advice) Bill 2011 and Corporations Amendment (Further Future of Financial Advice Measures) Bill 2011, made specific recommendations about the need to monitor the quality of advice about the sale of life insurance.

Policy developments

Report 413

- 6 Poor quality personal advice and sales practices in relation to retail life insurance have been an issue in ASIC investigations and surveillances over many years. In 2014, ASIC undertook a surveillance to understand the personal advice consumers were receiving about life insurance and to identify opportunities to promote personal life insurance advice that is in the best interests of the client.
- 7 ASIC published Report 413 *Review of retail life insurance advice* (REP 413) in October 2014, which presents the findings from this surveillance.
- 8 We found unacceptable levels of poor quality advice, and a strong correlation between high upfront commissions and poor consumer outcomes,

including in situations where the recommendation was to switch products. We found that 37% of the advice we reviewed failed to comply with the laws in force at the time the advice was given.

Note: In collecting data during our surveillances, we found that life insurers used several different types of remuneration models, including:

- *high upfront commission*—generally an upfront commission of 100% to 130% of the new business premium and an ongoing commission of around 10% of renewal premiums;
- *hybrid commission*—generally an upfront commission of 70% of the new business premium and an ongoing commission of around 20% of renewal premiums;
- *level commission*—generally a flat-rate upfront commission of around 30% of the new business premium and an ongoing commission of around 30% of renewal premiums; and
- *no commission*—includes fee-for-service remuneration arrangements, and any commission paid by the life insurer to the adviser is rebated back to the client.

- 9 We reviewed advice that was given both before the FOFA reforms (47% of files) and after FOFA (53% of files). For pre-FOFA advice, we rated the advice against the obligation to give appropriate advice (the test in s945A of the Corporations Act that applied at the time). For post-FOFA advice, we rated the advice by reference to the following conduct obligations:
- (a) to act in the best interests of the client (s961B);
 - (b) to give appropriate advice (s961G); and
 - (c) to give priority to the interests of the client in the event of a conflict of interest (s961J).
- 10 The factors we identified that affected the quality of advice were:
- (a) adviser incentives;
 - (b) inappropriate scaling of advice;
 - (c) lack of strategic life insurance advice;
 - (d) weak rationales for product replacement advice; and
 - (e) failure to consider the relationship between life insurance and superannuation.
- 11 We made a number of recommendations for insurers, AFS licensees, advisers and their professional associations, including a focus on how to ensure that client interests were met and balancing the issue of affordability versus cover. We also recommended that insurers change their remuneration arrangements and develop simpler products, while advisers should review their business models to address structural barriers to the provision of compliant life insurance advice.
- 12 Industry responded to REP 413 by establishing the Life Insurance and Advice Working Group (LIAWG), chaired by John Trowbridge, a former member of the Australian Prudential Regulation Authority (APRA).

Trowbridge report

- 13 Following the publication of REP 413, the LIAWG commissioned its own review of retail life insurance advice. The findings of the review are set out in *Review of retail life insurance advice* (Trowbridge report), published in March 2015. The review found problems in the remuneration structures for advisers and poor quality of personal advice to retail clients by advisers, as well as poor consumer understanding of the advice and products they were being sold.
- 14 The Trowbridge report proposed a new ‘reform model’ for adviser remuneration with a three-year transition period. Under the proposed reform model, commission payments would transition to a level commission rate of 20% of premiums, plus a one-off advice payment payable once every five years on a per client basis.
- 15 The Trowbridge report also included measures to improve the quality of advice, and address other adviser incentives, insurer practices, product offerings, and industry productivity.

Financial System Inquiry

- 16 The Financial System Inquiry (FSI) was commissioned by the Government in December 2013 and chaired by David Murray, with the objective of examining how the financial system could be positioned to best meet Australia’s evolving needs and support Australia’s economic growth. The FSI published its final report on 7 December 2014.
- 17 In looking at consumer outcomes as part of the terms of reference, the FSI considered life insurance and whether consumers were being treated fairly under the current arrangements with advisers. The FSI raised concerns about high upfront commissions and the misalignment of financial incentives with consumer outcomes.
- 18 In its final report, the FSI recommended a level commission structure to better align the interests of advisers and consumers. The FSI did not recommend banning commissions altogether, because it considered this might have the effect of dissuading some consumers, who did not want to pay advisers a service fee, from buying life insurance.
- 19 However, the FSI recommended² that the Government revisit the option of banning commissions entirely if the issues in this sector did not improve. The FSI also recommended that the Government consider the findings of the LIAWG.

² Recommendation 24, ‘Align the interests of financial firms and consumers’, Financial System Inquiry, final report, December 2014.

Implementation of the reform proposals

- 20 In response to the recommendations made in the Trowbridge report, the Government called on industry to develop its own reforms to address the problems in the life insurance advice sector.
- 21 The Government responded to the FSI final report on 20 October 2015. In response to the FSI's recommendation to impose a level commission structure for life insurance advice, the Government agreed that reform in this area was needed, but chose to support the industry's reform proposals—key elements of which are outlined in paragraphs 23 and 24.
- 22 On 6 November 2015, the Minister for Small Business and Assistant Treasurer, the Hon Kelly O'Dwyer, announced the proposed final industry package of reforms to commence on 1 July 2016 (reform package). The announcement referred to the consensus reached by industry on the implementation of important improvements to the remuneration arrangements in the retail life insurance sector. It noted that the reform package would commence on 1 July 2016 and would apply to personal and general advice including direct sales channels.
- 23 The proposals on commissions and remuneration of advisers included:
- (a) a reduction in upfront commissions—starting with a maximum upfront commission of 80% of the first year premium to apply from 1 July 2016, decreasing to a maximum upfront commission of 60% of the first year premium to apply from 1 July 2018. Ongoing commission would be set at 20% from 1 July 2016;
 - (b) clawback over two years to apply from 1 July 2016 as follows:
 - (i) if a policy lapses or the premium decreases in the first year of the policy, the amount of commission to be repaid is calculated with reference to 100% of the commission on the first year's premium; and
 - (ii) if a policy lapses or the premium decreases in the second year of the policy, the amount of commission to be repaid is calculated with reference to 60% of the commission on the first year's premium;
 - (c) a ban on other forms of conflicted remuneration, consistent with the FOFA reforms, to apply from 1 July 2016; and
 - (d) life insurers to offer fee-for-service insurance products for advisers who wish to operate on a fee-for-service basis.

24 The transitional arrangements are set out in Table 1:

Table 1: Transitional arrangements—Government reform proposals

Date	Maximum total upfront commission
From 1 July 2016	80% of the premium in the first year of the policy
From 1 July 2017	70% of the premium in the first year of the policy
From 1 July 2018	60% of the premium in the first year of the policy

25 The Government also announced further proposals, including:

- (a) a life insurance code of conduct to be developed by the Financial Services Council by 1 July 2016;
- (b) industry to have responsibility for widening approved product lists through the development of a new industry standard;
- (c) ongoing reporting to ASIC by life insurers of policy replacement data to commence from 1 July 2016;
- (d) ASIC to conduct a review of the impact of the life insurance reforms by the end of 2018; and
- (e) ASIC to commence a review of Statements of Advice (SOAs) in the second half of 2016, with a view to making disclosure simpler and more effective for consumers as well as assisting advisers to make better use of these documents. The review of SOAs would also consider whether the disclosure of adviser remuneration could be more effective, including prominent upfront disclosure of commissions.

26 The Government proposes to amend the Corporations Act to facilitate the rationalisation of legacy products in the life insurance and managed investment sectors, with further analysis of the taxation implications explored in the context of the Government's taxation white paper process.

27 On 3 December 2015, the Government released draft legislative amendments and draft explanatory material to seek feedback on the method of implementing some aspects of the reform package. The Government proposes to amend the Corporations Act to:

- (a) remove the exemption for life insurance advice from the ban on conflicted remuneration under s963B(1)(b)—this means that benefits (commissions) paid in relation to life insurance products would generally be considered conflicted remuneration and therefore be prohibited; and

Note: As set out in paragraph 28(b), level commissions will still be permitted

- (b) enable ASIC, through a legislative instrument, to permit benefits (commissions) to be paid, if requirements are met relating to:
 - (i) the maximum level of commission paid compared to the premium³ payable (referred to as the ‘acceptable ratio’ in s963BA of the draft legislative amendments); and
 - (ii) clawback arrangements (i.e. the amount of upfront commission an advice licensee or its representatives must repay to a life insurer under certain circumstances).

28 The draft legislative amendments also cover:

- (a) the scope of the proposals (i.e. the proposals apply to the sale of life insurance through personal and general advice);
- (b) level commissions (i.e. the draft legislative amendments permit benefits to be paid if the ratio between the benefit, or commission, and the premium—referred to as the ‘relevant amount’ payable for the product—is the same for the year in which the product is issued as it is for each year in which the product is renewed);

Note: The term ‘relevant amount’ is defined in s963B of the draft amendments.

- (c) the ‘clawback’ provisions (i.e. when an AFS licensee or its representatives must repay benefits paid by a life insurer);
- (d) the ‘grandfathering’ provisions (i.e. transitional arrangements that allow some commissions and volume-based payments to be made under pre-existing arrangements for pre-existing policies); and
- (e) the amendment of s912C of the Corporations Act (i.e. to provide that ASIC may require information to be given to us in a specified manner, including electronically).

29 The proposals in this consultation paper need to be read in the context of the Government’s proposed legislative amendments, available on the [Treasury website](#).

30 If the Bill becomes law in the form set out in the proposed legislative amendments, we propose to make an instrument specifying:

- (a) the acceptable ratio, or way of working out the ratio, between the benefit payable to a life insurance adviser and the amount payable for the product to which the benefit relates (i.e. setting a maximum level of upfront and ongoing commissions to be paid to advisers); and
- (b) the amount, or way of working out the amount, that is an acceptable repayment of benefits paid by the insurer (i.e. ‘clawback’).

³ The term ‘premium’ includes the premium payable for the policy and any fees payable (e.g. policy fee and frequency loading), but excludes taxes imposed by the Commonwealth, or state or territory (e.g. GST and stamp duty), in line with the definition of ‘relevant amount’ in the draft legislative amendments: see s963B.

- 31 We are also consulting on the data we propose should be reported to ASIC on an ongoing basis. We will exercise our power under s912C to issue notices to require the relevant information.
- 32 We propose that these measures will take effect on 1 July 2016, which aligns with the proposed start date of the amendments to the Corporations Act in the Government's proposed legislative amendments.
- 33 The proposed measures are designed to bring about better outcomes for consumers by removing the incentive for advisers to rewrite life insurance policies in order to benefit from high upfront commissions.
- 34 ASIC will conduct a review in 2018. The Minister for Small Business and Assistant Treasurer, the Hon Kelly O'Dwyer said:
- If the 2018 review does identify significant improvement, the Government will move to mandate level commissions, as was recommended by the Murray Inquiry [FSI].
- Note: See the [media release](#) *Government announces significant improvements to life insurance industry*, on 6 November 2015, by the Minister for Small Business and Assistant Treasurer, the Hon Kelly O'Dwyer.
- 35 This consultation paper sets out the policy we propose to give effect to in the legislative instrument, and the information we propose to require from AFS licensees by issuing notices under s912C. We ask a series of questions to assist us in developing the instrument and notices.

B Setting a maximum level of commission

Key points

If the Government amends the Corporations Act by enabling ASIC to make a legislative instrument to set a maximum level of commission to be paid by life insurers to advisers, we propose to make an instrument giving effect to the reform package.

Under the terms of the instrument, we propose that, if a life insurer adopts an upfront or hybrid commission model, the commission levels would be set at:

- a maximum of 60% of the premium in the first year of the policy; and
- a maximum ongoing commission of 20% of the premium in all subsequent years.

We propose a transition period of two years to allow businesses to move smoothly to the new regime.

Our proposed requirements

Proposal

B1 If the Government amends the Corporations Act to enable ASIC to determine in a legislative instrument the ratio (or a way of working out the ratio) between the benefit payable to the adviser and the relevant amount payable for the product (i.e. a maximum level of commission to be paid by life insurers to advisers), we propose to make an instrument giving effect to the reform package.

Under the terms of the instrument, we propose that, from 1 July 2018, if a life insurer adopts an upfront or hybrid commission model:

- the level of commissions will be set at a maximum of 60% of the premium in the first year of the policy; and
- an ongoing commission for policy renewals will be set at a maximum of 20% of the total of the premium paid for the renewal.

We propose a transition period of two years, commencing on 1 July 2016, as set out in Table 2.

Table 2: Transitional arrangements—Maximum commission levels

Date	Maximum total upfront commission
From 1 July 2016	80% of the premium in the first year of the policy
From 1 July 2017	70% of the premium in the first year of the policy
From 1 July 2018	60% of the premium in the first year of the policy

Note: The term 'premium' includes the premium payable for the policy and any fees payable (e.g. policy fee and frequency loading), but excludes taxes imposed by the Commonwealth, or a state or territory (e.g. GST and stamp duty), in line with the definition of 'relevant amount' in the draft legislative amendments: see s963B.

Your feedback

B1Q1 Are there any considerations ASIC should take into account in implementing this proposal?

B1Q2 How do you think any increase in premium should be dealt with under the proposed commission structure?

(a) For example, if the premium increases in the second year because the amount insured has increased, should the maximum upfront commission apply to the amount by which the premium has increased?

(b) Are there any circumstances where the maximum upfront commission should or should not apply where there is an increase in premium in subsequent years? Please specify those circumstances.

Rationale

36 The findings in REP 413 showed a strong, positive correlation between high upfront commissions and poor advice. In addition, the FSI also considered that the interests of financial advisers were misaligned with the interests of consumers.

37 The impact of poor advice affects consumers directly and indirectly. Direct effects include:

- (a) consumers paying for life insurance that is too expensive (which, in turn, can lead to loss of cover);
- (b) inappropriate depletion of superannuation balances by high premiums (examples of which were identified in REP 413); or
- (c) loss of cover.

38 Indirect effects include:

- (a) higher overall premiums due to costs associated with greater lapse rates arising from high upfront commissions; or
- (b) consumers buying inappropriate products directly from the life insurer without seeking advice about what is most appropriate for their circumstances.

39 The reform package does not eliminate conflicts of interest in remuneration, given that an upfront commission of 60% of the first year's premium will still be permitted.

40 However, the reforms balance the competing interests of advisers and clients. Setting a maximum level of 60% of the total premium in the first year of the policy will:

- (a) allow advisers to be remunerated for their upfront costs in providing advice to a client; and

- (b) ensure that consumers are still able to access life insurance advice, while reducing the incentive for advisers to recommend that their clients switch life insurance products unnecessarily.

41 A two-year transition period allows AFS licensees to manage their business and promotes a smooth transition to the new commission regime.

C Clawback arrangements

Key points

If the Government amends the Corporations Act by enabling ASIC to determine in a legislative instrument the amount (or a way of working out the amount) of benefits to be repaid by advisers to life insurers if the policy is cancelled or the premium is reduced, we propose to make an instrument to give effect to the reform package.

Under the terms of the instrument, we propose that, if a life insurer pays commission other than under a level commission arrangement, and 'clawback' is triggered:

- in the first year of the policy—100% of the commission paid in the first year will be repaid to the life insurer; and
- in the second year of the policy—60% of the commission paid in the first year will be repaid to the life insurer.

This proposal is intended to remove the incentive for advisers to inappropriately rewrite new business within a two-year period, which will lead to better outcomes for consumers.

Our proposed requirements

Proposal

- c1 If the Government amends the Corporations Act to enable ASIC to determine in a legislative instrument the amount (or a way of working out the amount) of benefits to be repaid by advisers to life insurers if the policy is cancelled or the premium is reduced (other than for suicide or self-harm), we propose to make a legislative instrument giving effect to the reform package.

We propose that, if a life insurer pays a commission other than under a level commission arrangement, and 'clawback' is triggered:

- (a) the repayment of commissions will be required over a two-year period, in the way set out in Table 3; and
- (b) if there is a reduction in premium, the repayment amount will relate to the amount of reduction in the premium, in the way set out in Table 3.

Note: Clawback will be required if, within two years of a life insurance policy being issued, the policy is cancelled or is not renewed (other than because of suicide or self-harm), or the premium is reduced: see the 'clawback requirements' in s963BA of the draft legislative amendments.

Table 3: Proposed clawback arrangements for life insurance policies that have lapsed

Policy year	If a policy is cancelled or is not renewed...	If the premium is reduced...
Year 1	<p>Advisers must repay 100% of the commission on the first year's premium.</p> <p><i>Example:</i> For a first year premium of \$1,000 and an upfront commission of \$600, repayment is \$600 (i.e. 100% x \$600).</p>	<p>Advisers must repay the proportion of the premium reduction applied to 100% of the commission received for the first year.</p> <p><i>Example:</i> For a first year premium of \$1,000 and an upfront commission of \$600, if the premium falls to \$500 in the first year (i.e. 50% reduction), repayment is \$300 (i.e. 100% x \$600 x 50%).</p>
Year 2	<p>Advisers must repay 60% of the commission on the first year's premium.</p> <p><i>Example:</i> For a first year premium of \$1,000 and an upfront commission of \$600, repayment is \$360 (i.e. 60% x \$600).</p>	<p>Advisers must repay the proportion of the premium reduction applied to 60% of the commission received for the first year.</p> <p><i>Example:</i> For a first year premium of \$1,000 and an upfront commission of \$600, if the premium falls to \$500 in the second year (i.e. 50% reduction), repayment is \$180 (i.e. 60% x \$600 x 50%).</p>

Note: The proposed clawback percentages shown in this table will be the minimum required by the ASIC instrument. Life insurers and advisers are able to enter into contractual agreements that have higher rates of clawback.

Your feedback

C1Q1 Are there any considerations ASIC should take into account in implementing this proposal?

Rationale

- 42 REP 413 reported a spike in policy lapse rates for all policy and premium types in the second year of a life insurance policy when clawback arrangements no longer applied. The findings in REP 413 showed that insurance sold through advice remunerated by high upfront commission models lapsed at a higher rate than other adviser remuneration models and, for stepped premiums, they remained persistently high.
- Note: A stepped premium policy is a policy where the premium is recalculated upon each renewal. The premium usually increases according to risk factors such as age.
- 43 Current clawback arrangements are generally in place for 12 months. This means there is no clear disincentive for advisers to recommend a new policy to clients after the end of the first year.
- 44 Frequent rewriting of policies can be costly for insurers too. As we noted in REP 413, insurers lose existing business at a point in the policy lifecycle where they have no prospect of recovering high upfront costs and, at the same time, insurers are incurring further upfront costs to win new business to replace business lost to competitors.

- 45 The proposal to impose a maximum commission level of 60% of the premium in the first year of the policy, together with the requirement to repay 100% of the commission if the policy lapses, is designed to reduce the incentive for advisers to inappropriately rewrite clients' policies. Increasing the period for clawback is intended to remove the incentive to rewrite the policy for at least two years, and reduces the level of the conflict of interest for the adviser.
- 46 Even though the reform package reduces the current levels of upfront commission to 60% of the first year's premium, we still consider the clawback arrangements are necessary. The combination of the cap on upfront commissions and the clawback of commission over a two-year period should bring about better quality advice, as it significantly reduces the incentive for advisers to inappropriately switch a client's policy.

D Ongoing reporting to ASIC

Key points

As part of the reform package, the Government announced that life insurers will be required to provide ongoing policy replacement data to ASIC, and that ASIC will conduct a review in 2018.

We propose to require detailed information on life insurance policies, remuneration, lapse rates and clawback amounts.

We intend to use this information as part of the review we will conduct in 2018 to establish whether the life insurance reforms have been effective in producing better outcomes for consumers, as well as to gain a better understanding of the industry in general.

Our proposed requirements

Proposal

- D1** We propose to use our information-gathering powers under s912C of the Corporations Act to require, by written notice, the following information from life insurers on life insurance sold through both personal and general advice, and also where there is no advice provided (i.e. direct sales):
- (a) information on life insurance policies, including:
 - (i) how many policies are in force;
 - (ii) details of the policies in force, such as:
 - the inception date on each policy;
 - how many policies are to ‘first time insureds’;
 - how many are new or altered policies sold to existing policy holders;
 - the type of policies (i.e. life, total and permanent disability, trauma, income protection and various combinations of these)
 - the structure of policies (including premiums and the sum insured); and
 - any trends in the structure of policies over time (e.g. an increase or decrease in premiums relative to the sum insured); and
 - (iii) how many policies have been exited (and the reasons for the exit).

Note: This will include historical data (i.e. going back two to five years).

- (b) remuneration data, including:
 - (i) historical data on commissions (where relevant);
 - (ii) the type of remuneration model adopted (i.e. upfront commission, hybrid commission, level commission, or no commission); and
 - (iii) the level of upfront and ongoing commissions being paid (where relevant);
- (c) lapse rates and clawback amounts, including:
 - (i) data on lapse rates;
 - (ii) the reasons for policies being exited (see also information required for policies in D1(a)(iii)); and
 - (iii) for every policy that lapsed, the amount that was clawed back; and
- (d) data on policies sold:
 - (i) with personal advice;
 - (ii) with general advice; or
 - (iii) with no advice.

We may specify in the notice how we would like the information to be provided to us (e.g. electronically).

We propose to remove any identifying details before publishing this information or releasing a final report.

Your feedback

- D1Q1 Are there any considerations ASIC should take into account in implementing this proposal?
- D1Q2 Is there information we have not covered that you think we should require? If so, please specify.
- D1Q3 Do you think we should also collect data at an adviser level?
- D1Q4 Do you have any feedback on our proposal to remove identifying details before we publish the information?
- D1Q5 What will be the costs for you to provide all of the information we have set out in this proposal? Please provide amounts in dollars, if possible. Are there particular types of information that are more difficult or costly to collect? If so, please provide details.
- D1Q6 What would be the costs for you to provide data on lapse rates and clawback arrangements only? Please provide amounts in dollars, if possible.
- D1Q7 Do you think we should be collecting historical information? If so, how many years of historical data should we collect?

- D2** The reform package envisages that ASIC will start collecting data from 1 July 2016. We propose that the information in proposal D1 is reported to us twice a year (i.e. starting on 1 July 2016 and then every six months subsequently).

Your feedback

- D2Q1 Are there any considerations ASIC should take into account in implementing this proposal?
- D2Q2 Does this timing allow you to adequately prepare your systems to start reporting on the specified data from 1 July 2016?

Rationale

- 47 Reporting the proposed information to ASIC will enable us to monitor changes in industry practices in response to the life insurance reforms, and to establish whether problems in the sector continue to exist. The information will be used as part of our review in 2018 of the effectiveness of the life insurance reforms. We plan to periodically publish the data we receive, after removing any identifying details, and to make the results of our review public. This will provide information to the industry as a whole about the impact of the reforms.
- 48 We want to see whether advisers are rewriting business for their clients in order to get the (still relatively high) upfront commissions in the transition period, or whether the reforms are effective in removing the incentive to rewrite policies, and in creating a better environment for advisers to give good quality advice to their clients.
- 49 We also want to obtain general information about life insurance policies and premiums so that we can better understand the trends in the life insurance sector, including in relation to distribution models and the overall impact of the reforms.

E Regulatory and financial impact

50 In developing the proposals in this paper, we have carefully considered their regulatory and financial impact. We have also considered the consultation and feedback we have received from industry throughout this process. On the information currently available to us, we think they will strike an appropriate balance between:

- (a) encouraging advisers to provide better quality advice (personal and general) to their clients on life insurance; and
- (b) ensuring that life insurers, AFS licensees and independent advisers do not incur unreasonable costs in providing advice that better aligns the interests of advisers and clients in accordance with the requirements in the ASIC instrument.

51 Before settling on a final policy, we will comply with the Australian Government's regulatory impact analysis (RIA) requirements by:

- (a) considering all feasible options, including examining the likely impacts of the range of alternative options which could meet our policy objectives;
- (b) if regulatory options are under consideration, notifying the Office of Best Practice Regulation (OBPR); and
- (c) if our proposed option has more than minor or machinery impact on business or the not-for-profit sector, preparing a Regulation Impact Statement (RIS).

52 All RISs are submitted to the OBPR for approval before we make any final decision. Without an approved RIS, ASIC is unable to give relief or make any other form of regulation, including issuing a regulatory guide that contains regulation.

53 To ensure that we are in a position to properly complete any required RIS, please give us as much information as you can about our proposals or any alternative approaches, including:

- (a) the likely compliance costs;
- (b) the likely effect on competition; and
- (c) other impacts, costs and benefits.

See 'The consultation process', p. 4.

Key terms

Term	Meaning in this document
advice	Financial product advice
advice provider	A person to whom the obligations in Div 2 of Pt 7.7A of the Corporations Act apply when providing personal advice to a client. This is generally the individual who provides the personal advice. However, if there is no individual that provides the advice, which may be the case if advice is provided through a computer program, the obligations in Div 2 of Pt 7.7A apply to the legal person that provides the advice (e.g. a corporate licensee or authorised representative)
adviser	An advice provider
AFS licence	An Australian financial services licence under s913B of the Corporations Act that authorises a person who carries on a financial services business to provide financial services Note: This is a definition contained in s761A.
AFS licensee	A person who holds an AFS licence under s913B of the Corporations Act Note: This is a definition contained in s761A.
APRA	Australian Prudential Regulation Authority
ASIC	Australian Securities and Investments Commission
authorised representative	A person authorised by an AFS licensee, in accordance with s916A or 916B of the Corporations Act, to provide a financial service or services on behalf of the licensee Note: This is a definition contained in s761A.
clawback	A commission or benefit that is paid to an adviser that is recovered, or 'clawed back', by the insurer if the policy lapses or the premium decreases within a certain period
client	A retail client
conflicted remuneration	A benefit given to an AFS licensee, or a representative of an AFS licensee, who provides financial product advice to clients that, because of the nature of the benefit or the circumstances in which it is given: <ul style="list-style-type: none"> • could reasonably be expected to influence the choice of financial product recommended by the licensee or representative to clients; or • could reasonably be expected to influence the financial product advice given to clients by the licensee or representative. <p>In addition, the benefit must not be excluded from being conflicted remuneration by the Corporations Act or Corporations Regulations</p>

Term	Meaning in this document
conflicted remuneration provisions	The provisions on conflicted remuneration and other banned remuneration in Divs 4 and 5 of Pt 7.7A of the Corporations Act and in Div 4 of Pt 7.7A of the Corporations Regulations
Corporations Act	<i>Corporations Act 2001</i> , including regulations made for the purposes of that Act
draft legislative amendments	The Government's draft legislative amendments and explanatory material containing proposed changes to the Corporations Act to: <ul style="list-style-type: none"> • remove the exemption from the conflicted remuneration provisions for life insurance advice; and • allow benefits to be paid to advisers if requirements imposed by ASIC are met
reform package	The final reform proposals developed by industry—to commence on 1 July 2016—that include proposals to improve the quality of advice in the life insurance industry through reforming the remuneration arrangements with advisers
financial product	A facility through which, or through the acquisition of which, a person does one or more of the following: <ul style="list-style-type: none"> • makes a financial investment (see s763B); • manages financial risk (see s763C); • makes non-cash payments (see s763D) <p>Note: This is a definition contained in s763A of the Corporations Act: see also s763B–765A.</p>
financial product advice	A recommendation or a statement of opinion, or a report of either of these things, that: <ul style="list-style-type: none"> • is intended to influence a person or persons in making a decision about a particular financial product or class of financial product, or an interest in a particular financial product or class of financial product; or • could reasonably be regarded as being intended to have such an influence. <p>This does not include anything in an exempt document.</p> <p>Note: This is a definition contained in s766B of the Corporations Act.</p>
FSI	Financial System Inquiry
FOFA	Future of Financial Advice
general advice	Financial product advice that is not personal advice <p>Note: This is a definition contained in s766B(4) of the Corporations Act.</p>

Term	Meaning in this document
grandfathered	A benefit to which the conflicted remuneration provisions do not apply because it is given under an arrangement entered into before 1 July 2013 (or before the date that an AFS licensee elects to comply with Pt 7.7A)
level premium policy	A policy where the premium is calculated at the start of the policy and remains fixed at the same level for the duration of the policy
LIAWG	Life Insurance and Advice Working Group
licensee	An AFS licensee
life insurance	A life risk insurance product, which is defined in s764A(1)(e) and means a life policy, or a sinking fund policy within the meaning of the <i>Life Insurance Act 1995</i> (Life Insurance Act), that is a contract of insurance. The definition excludes payments by employee associations, certain payments under the Life Insurance Act, funeral benefits and employee benefits paid by employers
life insurers	Life insurance providers
personal advice	Financial product advice given or directed to a person (including by electronic means) in circumstances where: <ul style="list-style-type: none"> the provider of the advice has considered one or more of the client's objectives, financial situation and needs; or a reasonable person might expect the provider to have considered one or more of these matters <p>Note: This is a definition contained in s766B(3) of the Corporations Act.</p>
Pt 7.7A (for example)	A part of the Corporations Act (in this example, numbered 7.7A)
REP 413	ASIC's Report 413 <i>Review of retail life insurance advice</i>
representative of an AFS licensee	Means: <ul style="list-style-type: none"> an authorised representative of the licensee; an employee or director of the licensee; an employee or director of a related body corporate of the licensee; or any other person acting on behalf of the licensee <p>Note: This is a definition contained in s910A of the Corporations Act.</p>
retail client	A client as defined in s761G of the Corporations Act and Div 2 of Pt 7.1 of the Corporations Regulations
retail life insurance	Life insurance
s782 (for example)	A section of the Corporations Act (in this example numbered 782), unless otherwise specified

Term	Meaning in this document
Statement of Advice (SOA)	A document that must be given to a client for the provision of personal advice under Subdivs C and D of Div 3 of Pt 7.7 of the Corporations Act Note: See s761A for the exact definition.
Trowbridge report	Report by John Trowbridge, <i>Review of retail life insurance advice</i> , published 26 March 2015

List of proposals and questions

Proposal	Your feedback
<p>B1 If the Government amends the Corporations Act to enable ASIC to determine in a legislative instrument the ratio (or a way of working out the ratio) between the benefit payable to the adviser and the relevant amount payable for the product (i.e. a maximum level of commission to be paid by life insurers to advisers), we propose to make an instrument giving effect to the reform package.</p> <p>Under the terms of the instrument, we propose that, from 1 July 2018, if a life insurer adopts an upfront or hybrid commission model:</p> <ul style="list-style-type: none"> (a) the level of commissions will be set at a maximum of 60% of the premium in the first year of the policy; and (b) an ongoing commission for policy renewals will be set at a maximum of 20% of the total of the premium paid for the renewal. <p>We propose a transition period of two years, commencing on 1 July 2016, as set out in Table 2.</p> <p>Note: The term 'premium' includes the premium payable for the policy and any fees payable (e.g. policy fee and frequency loading), but excludes taxes imposed by the Commonwealth, or a state or territory (e.g. GST and stamp duty), in line with the definition of 'relevant amount' in the draft legislative amendments: see s963B.</p>	<p>B1Q1 Are there any considerations ASIC should take into account in implementing this proposal?</p> <p>B1Q2 How do you think any increase in premium should be dealt with under the proposed commission structure?</p> <ul style="list-style-type: none"> (a) For example, if the premium increases in the second year because the amount insured has increased, should the maximum upfront commission apply to the amount by which the premium has increased? (b) Are there any circumstances where the maximum upfront commission should or should not apply where there is an increase in premium in subsequent years? Please specify those circumstances.
<p>C1 If the Government amends the Corporations Act to enable ASIC to determine in a legislative instrument the amount (or a way of working out the amount) of benefits to be repaid by advisers to life insurers if the policy is cancelled or the premium is reduced (other than for suicide or self-harm), we propose to make a legislative instrument giving effect to the reform package.</p> <p>We propose that, if a life insurer pays a commission other than under a level commission arrangement, and 'clawback' is triggered:</p> <ul style="list-style-type: none"> (a) the repayment of commissions will be required over a two-year period, in the way set out in Table 3; and (b) if there is a reduction in premium, the repayment amount will relate to the amount of reduction in the premium, in the way set out in Table 3. <p>Note: Clawback will be required if, within two years of a life insurance policy being issued, the policy is cancelled or is not renewed (other than because of suicide or self-harm), or the premium is reduced: see the 'clawback requirements' in s963BA of the draft legislative amendments.</p>	<p>C1Q1 Are there any considerations ASIC should take into account in implementing this proposal?</p>

Proposal	Your feedback
<p>D1 We propose to use our information-gathering powers under s912C of the Corporations Act to require, by written notice, the following information from life insurers on life insurance sold through both personal and general advice, and also where there is no advice provided (i.e. direct sales):</p> <p>(a) information on life insurance policies, including:</p> <ul style="list-style-type: none"> (i) how many policies are in force; (ii) details of the policies in force, such as: <ul style="list-style-type: none"> – the inception date on each policy; – how many policies are to ‘first time insureds’; – how many are new or altered policies sold to existing policy holders; – the type of policies (i.e. life, total and permanent disability, trauma, income protection and various combinations of these) – the structure of policies (including premiums and the sum insured); and – any trends in the structure of policies over time (e.g. an increase or decrease in premiums relative to the sum insured); and (iii) how many policies have been exited (and the reasons for the exit). <p>Note: This will include historical data (i.e. going back two to five years).</p> <p>(b) remuneration data, including:</p> <ul style="list-style-type: none"> (i) historical data on commissions (where relevant); (ii) the type of remuneration model adopted (i.e. upfront commission, hybrid commission, level commission, or no commission); and (iii) the level of upfront and ongoing commissions being paid (where relevant); <p>(c) lapse rates and clawback amounts, including:</p> <ul style="list-style-type: none"> (i) data on lapse rates; (ii) the reasons for policies being exited (see also information required for policies in D1(a)(iii)); and (iii) for every policy that lapsed, the amount that was clawed back; and <p>(d) data on policies sold:</p> <ul style="list-style-type: none"> (i) with personal advice; (ii) with general advice; or (iii) with no advice. <p>We may specify in the notice how we would like the information to be provided to us (e.g. electronically).</p> <p>We propose to remove any identifying details before publishing this information or releasing a final report.</p>	<p>D1Q1 Are there any considerations ASIC should take into account in implementing this proposal?</p> <p>D1Q2 Is there information we have not covered that you think we should require? If so, please specify.</p> <p>D1Q3 Do you think we should also collect data at an adviser level?</p> <p>D1Q4 Do you have any feedback on our proposal to remove identifying details before we publish the information?</p> <p>D1Q5 What will be the costs for you to provide all of the information we have set out in this proposal? Please provide amounts in dollars, if possible. Are there particular types of information that are more difficult or costly to collect? If so, please provide details.</p> <p>D1Q6 What would be the costs for you to provide data on lapse rates and clawback arrangements only? Please provide amounts in dollars, if possible.</p> <p>D1Q7 Do you think we should be collecting historical information? If so, how many years of historical data should we collect?</p>

Proposal	Your feedback
D2 The reform package envisages that ASIC will start collecting data from 1 July 2016. We propose that the information in proposal D1 is reported to us twice a year (i.e. starting on 1 July 2016 and then every six months subsequently).	D2Q1 Are there any considerations ASIC should take into account in implementing this proposal? D2Q2 Does this timing allow you to adequately prepare your systems to start reporting on the specified data from 1 July 2016?
