ASIC Consultation Paper 294 – The sale of add-on insurance and warranties through car yard intermediaries

Submission by Legal Aid Queensland

TRIM no 2017/940612

The sale of add-on insurance through car yard intermediaries

Introduction

Legal Aid Queensland (LAQ) welcomes the opportunity to make a submission in response to ASIC Consultation Paper 294 – The sale of add-on insurance and warranties through car yard intermediaries. LAQ provides input into State and Commonwealth policy development and law reform processes to advance its organisational objectives. Under the *Legal Aid Queensland Act 1997*, LAQ is established for the purpose of "giving legal assistance to financially disadvantaged persons in the most effective, efficient and economical way" and is required to give this "legal assistance at a reasonable cost to the community and on an equitable basis throughout the State". Consistent with these statutory objects, LAQ contributes to government policy processes about proposals that will impact on the cost-effectiveness of LAQ's services, either directly or consequentially through impacts on the efficient functioning of the justice system.

LAQ always seeks to offer policy input that is constructive and is based on the extensive experience of LAQ's lawyers in the day to day application of the law in courts and tribunals. We believe that this experience provides LAQ with valuable knowledge and insights into the operation of the justice system that can contribute to government policy development. LAQ also endeavours to offer policy options that may enable government to pursue policy objectives in the most effective and efficient way.

LAQ's Consumer Protection Unit lawyers have extensive experience providing specialist advice and representation to vulnerable clients in consumer law matters. The unit provides advice to clients as well as lawyers and financial counsellors throughout Queensland in relation to mortgage stress, housing repossession, debt, contracts; loans; telecommunications and unsolicited consumer agreements.

LAQ regularly assists and represents clients who have legal problems as a result of the sale of add-on insurance and warranties through car yard intermediaries. This submission is informed by that knowledge and experience.

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Proposal 1 – Deferred Sales Model for Add-on products

Deferred sales model

Proposal: E1 We propose that the sale of add-on products by car yard intermediaries for a new or used car should be permitted only after a certain period of time has elapsed (the deferral period). During the deferral period: (a) providers would be restricted from offering, or entering into, a contract for an add-on product with a consumer; (b) car yard intermediaries would be restricted from: (i) arranging for a consumer to apply for an add-on product; or (ii) referring a consumer to a product provider in relation to an add-on product; and (c) consumers would be restricted from initiating the purchase of an add-on product directly with the provider, or opting-out of the deferral period.

E1Q1 Do you consider that it is appropriate to apply a deferral period to the sale of add-on products by car yard intermediaries? E1Q2 To what extent would a deferral address the consumer harms identified in this market?

LAQ supports the introduction of a deferral period to the sale of add-on products by car yard intermediaries. In assisting vulnerable consumers LAQ sees the following harms caused by the sale of add-on insurance products by car yard intermediaries:

(a) Consumers are not aware that they have been sold add-on insurance products.
(b) Consumers are sold products that are not suitable or necessary for them e.g. insurance cover significantly higher than the replacement value of the car.
(c) Consumers are sold products which they could never claim the benefit of e.g. Pensioners sold unemployment insurance.
(d) Consumers are sold poor value products.
(e) Consumers have often been kept at the car yard for many hours as part of the sales process before the issue of insurance is raised. In these circumstances consumers will often agree to any product that is offered to them in order to finalise the sales process.
(f) Add on insurance products can be marketed as a standard part of any car purchase rather than an optional extra to the purchase.
(g) Add on insurance products are complex and often poorly explained by car yard intermediaries.
(h) Products are sold to consumers on the basis of the commission earned by the salesperson and not the suitability of the product.

The introduction of a deferred sales model will address these issues because:

(a) Consumers will have an opportunity to consider information provided to them about the product away from the pressure of the car yard sales environment.
(b) Consumers will have an opportunity to consider the value and suitability of the insurance away from the pressurised environment of the car yard sales process.
(c) Consumers will have an opportunity to assess whether, in their circumstances, they are likely to make a claim on any particular product.
(d) Consumers will have an opportunity to assess whether their existing insurance products provide them with adequate insurance protection.
(e) If they require insurance, consumers will have an opportunity to shop around and assess which product is suitable for their needs.

E1Q3 How would the proposal affect businesses (e.g. insurers, car dealers, finance brokers, credit providers)? Would it have a different impact on small businesses?

In LAQ's submission, the model is likely to require businesses, including insurers and car dealers to change their sales processes. However, the benefit provided to all consumers, particularly vulnerable consumers, from changing the current sales processes significantly outweighs any extra costs associated from businesses having to change their process.

E1Q4 Would the model need to apply differently to the new and used cars markets? In what ways could the model differ to be effective across the two markets?

In LAQ's experience, add on insurance products cause significant harm to consumers when they are sold in both the new and used car markets. LAQ sees no reason why the model should apply differently between the two markets.

E1Q5 What are the preconditions for a competitive online market? How can a deferred sales model contribute to this outcome?

In LAQ's view it is important that information about add on insurance products be provided in both on-line and other formats. The reason for this is that solely focusing on an on-line market risks excluding from the market:

(a) Those more vulnerable people, who for reasons of cost or access, do not have regular and easy access to the internet; and
(b) Those people who do not have the on-line skills to confidently access the internet.

The important pre-conditions for any market including an on-line market are:

(a) Availability of information;
(b) Access and awareness of all products available in the market; and
(c) The ability to easily compare relevant features of products, including coverage and price.

A deferred sales model can contribute to this outcome by allowing consumers:

(a) The ability to receive information about products in an easily assessable form;
(b) Time to research and compare relevant features of insurance products. It is important that any comparison websites developed to facilitate this comparison provide coverage of all products in the market or make clear to consumers the extent of the site's coverage of products.
(c) Time to assess the relevance of add on insurance products to their individual circumstances.

E1Q6 Could the objectives of a deferred sales model be achieved in a different way or could any complementary measures better ensure our objectives are achieved?

LAQ supports the deferred sales model as the most appropriate way of reducing the current consumer detriment caused by the sale of add on insurance products through car yard intermediaries.

E1Q7 If a deferred sales model was introduced, are there any existing related obligations on insurers, finance providers and car dealers that would no longer be appropriate and could be removed?

In LAQ's submission, the deferred sales model is attempting to address a consumer detriment that is not currently addressed by existing obligations. As a result, LAQ is not aware of any existing obligations that could be removed through the introduction of the deferred sales model.

E1Q8 What is the most effective way of testing whether consumer understanding has improved due to a deferred sales model? What metrics would provide the best way of measuring consumer comprehension?

LAQ acknowledges the difficulty in assessing improved consumer comprehension and understanding of add on insurance products. In LAQ's view one metric that could be used to assess improved consumer understanding is the successful claim rates made under each type of add on insurance. If a higher percentage of premiums paid by consumers are paid out in claims this is indicative of the fact that consumers have a better understanding of the products offered and are making better decisions about whether the products are suitable for them.

E1Q9 Should a consumer opt-out mechanism be included?

LAQ does not support the introduction of a consumer opt-out mechanism. It would cause significant and widespread detriment to the most vulnerable, disadvantaged and less financially aware consumers in our society.

The risks associated with an opt-out mechanism include:

(a) Vulnerable consumers being pressured by salespeople to exercise the opt-out mechanism even if it is not in their interests.
(b) It is very difficult to monitor what consumers are told by salespeople about their legal rights if the consumer exercises the opt-out mechanism.
(c) None of the current problems with the sale of add on insurance products would be addressed if an opt out mechanism was made available to consumers.

Commencement of the deferral period

Proposal: E1.1 We do not propose in this paper a specific trigger event for the commencement of the deferral period and seek stakeholders' views on this. The period could commence when the consumer: (a) receives a consumer communication (with mandated content); (b) finalises the vehicle purchase and receives the consumer communication; or (c) takes delivery of the vehicle and receives the consumer communication.

E1.1Q1 Which of the proposed options in paragraph 193 for commencement of the deferral period would be preferable and why (please suggest other options if relevant)? E1.1Q2 Which sales sequence (see Figure 1) is most likely to meet our stated objectives, and why?

LAQ supports the proposed Option B and Sales sequence B as the most preferable options to address the consumer detriment caused by the current add on insurance sales process.

The reasons for this are:

(a) It gives a consumer the opportunity to assess, separately to the car purchase and questions of finance, their need for any add on insurance products based on their individual circumstances.
(b) It gives consumers an opportunity to source insurance products that are not financed, which reduces the overall costs of the insurance products and improves their affordability.
(c) It allows the consumer to assess the information provided to them about add on insurance products away from the pressure of the car yard and financiers.
(d) It allows the consumer to make decisions about insurance that is suitable for their needs, knowing the vehicle that they have purchased.
(e) It may increase the amount of information available on-line about add on insurance products and see a market develop on-line for add on insurance products.
(f) It may encourage competition between insurers offering add-on insurance products.

E1.1Q3 How could the point at which the deferral period commences be easily documented to be readily verified by all relevant parties?

In LAQ's view, the deferral period should begin with either:

(a) The date on which mandated consumer information about add on insurance products is provided to the consumer; or
(b) The date on which the vehicle is delivered.

E1.1Q4 If the deferral period commenced at vehicle delivery, could short-term 'bridging' insurance be offered to cover the deferral period (only)? What does insurers' claims data demonstrate about the likelihood of a claim shortly after delivery?

In light of the availability of comprehensive car insurance and compulsory third party insurance, LAQ believes the risk of a consumer being uninsured during the deferral period is very small. The need for short term bridging insurance is unlikely and creates the risk of the same poor sales practices that are currently seen during the sale of add on insurance products through car yard intermediaries being used in any bridging insurance market.

Duration of the deferral period

Proposal: E1.2 We propose that the total duration of the deferral period for add-on products (except those discussed in proposal E1.4) could be a: (a) minimum of four days; and (b) maximum of 30 days.

E1.2Q1 What would be the appropriate duration of the deferral period within the range of 4–30 days and why?

LAQ supports introducing a 14 day deferral period for add on insurance products. In LAQ's submission, 14 days:

(a) Allows consumers sufficient time to consider all available information about add on insurance products.
(b) Allows consumers time to assess the relevance of add on insurance products to their individual needs.

(c) Is close enough to the original finance and purchase of the vehicle that the consumer is making the decision about purchasing the vehicle in the context of their original purchases.

E1.2Q2 Should the duration of the deferral period be different for new and used cars?

LAQ sees no basis for creating a different deferral period for new and used cars. If different deferral periods were adopted, it would just create unnecessary confusion for consumers.

E1.2Q3 What is the average period of time between the sale of a new car or a used car and its delivery to the consumer? What is the shortest period of time and how common is it?

LAQ has no quantitative data on the average time period between the sale of a new car or used car and its delivery to consumers. However, from dealing with vulnerable clients, LAQ is aware of a number of clients driving the car they have bought on the same day or the day after the purchase.

E1.2Q4 What is the average period of time between when a consumer applies for finance and approval? What is the shortest period of time and how common is it?

LAQ has no quantitative data on the average time period between a consumer applying for and being approved for finance. However, from dealing with vulnerable clients, LAQ is aware of a number of clients receiving same day finance approval.

Consumer Communication

Proposal: E1.3 We propose that the consumer communication should: (a) address the current limitations in consumers making informed decisions (as discussed in Section C); (b) include information about each type of add-on product being offered through the car dealership (e.g. in a standardised format) and how they interact with other elements of the transaction; (c) provide information to consumers that is accessible and addresses different levels of comprehension or financial literacy; and (d) make use of innovative techniques to deliver this information to the consumer.

E1.3Q1 Should providers be required to take active steps to ensure consumers read and understand information about their products before they can buy them? E1.3Q2 What forms of innovative disclosure could be used to better inform consumers about their insurance decision?

LAQ supports a model that does not rely solely on consumers being given information as sufficient compliance. In LAQ's experience, there is a real risk that consumers will not read or access the information provided to them.

LAQ supports the idea of interactive disclosure through an on-line app which could allow insurers to test a consumer's understanding of a product before the consumer purchases. This approach may ensure that consumers can be shown to better understand the products that they are signing up to.

However, for the reasons outlined in LAQ's answer to E1Q5, an on-line app may not be a suitable approach for all consumers and it is important that similar non on-line alternatives are also developed.

E1.3Q3 What information should the consumer communication include?

In LAQ's view, the most important consideration is that communication needs for consumers will be different depending on their existing financial literacy and numeracy skills. As a result, LAQ supports a similar obligation to Clause 7.2 of the Life Insurance Code of Practice being placed on providers offering add on insurance products to provide tailored consumer information based on the consumer's individual needs and financial literacy and numeracy skills.

If tailored information is not required, LAQ is concerned that vulnerable consumers, who often have lower financial literacy and numeracy, remain at risk from being signed up to inappropriate add on insurance products.

E1.3Q4 Should providers be required to inform consumers about the availability of other products that provide similar cover, but may be cheaper?

LAQ refers to the findings of ASIC Rep 471 - "The sale of life insurance through car dealers" which highlighted, amongst other problems, that the cost of life cover under CCI products sold through car yard intermediaries is more costly than the price of a term life product.

One of the reasons for this is that it is very difficult for consumers purchasing insurance products through car yard intermediaries to compare the value of products sold through car yards to those products sold outside of car yards.

As a result, LAQ supports a requirement that providers be required to inform consumers about the availability of other products that provide similar cover. This approach is likely to:

(a) encourage providers to offer more competitively priced products; and
(b) encourage consumers to shop around before buying a product.

E1.3Q5 If so, what information should the consumer communication include?

In LAQ's view, the information that the consumer communication should include is:

(a) A list of alternative products that may provide equal, similar or better coverage, and
(b) how these alternate products can be accessed by the consumer.

Mechanical Breakdown insurance and warranties

Proposal: E1.4 Where these products are sold with new cars or used cars that are still covered by the manufacturer's warranty, we consider that: (a) a different deferral period could apply; and (b) the consumer communication could be tailored to explain that cover will not commence for some time and set out the consequent risks in buying the product.

E1.4Q1 Should a separate deferred sales model be introduced for these products? If not, how could the particular risks associated with these products be addressed?

LAQ does not support mechanical risk products being sold with new or used cars that are covered by a manufacturer's warranty.

The reasons for this are:

(a) It is impossible for consumers to assess the value of a product whose coverage may not start to apply for years after it is purchased;
(b) A consumer may sell the car before the coverage begins;
(c) The coverage provided by a mechanical risk policy may prevent a consumer making a claim under it.

The fundamental flaws with this product cannot be cured by any deferred sales model.

Proposal 2 – Enhanced supervision obligations for product providers

Proposal: E2 We propose to introduce specific requirements for the supervision and monitoring of a provider's authorised representatives, based on the risks for consumers in this distribution channel.

E2Q1 Given the limitations in monitoring conduct at the point of sale, what changes would be necessary to ensure providers are effectively supervising their representatives? E2Q2 What risk indicators could be introduced to improve the capacity of providers to monitor their representatives?

In LAQ's submission the introduction of a deferred sales model is likely to assist providers to effectively supervise their representatives because it will provide a standardised process for the sale of add on insurance products.

LAQ also supports the development of minimum requirements on supervision for insurers and product providers which can be informed and developed by the risk indicators set out in Paragraphs 257 and 258 of ASIC Consultation Paper 294.

E2Q3 What sanctions would be most effective in deterring representatives from engaging in unfair practices at the point of sale?

In LAQ's view the following sanctions would be effective in deterring unfair practices by sales representatives:

(a) Removing the representative's authorisation to sell add on insurance products.
(b) Clawing back commission paid as a result of insurance products entered into through unfair practices.
(c) Proactively identifying affected consumers and paying them compensation.
(d) Reduce the amount of commissions paid by insurers to sales representatives.
(e) Commissions paid to sales representatives should not just solely be based on the sale of an add-on insurance product.