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The FBAA being the leading professional industry association to finance and mortgage brokers nationally, welcomes the opportunity to make a submission in response to ASIC's Consultation Paper 294: The sale of add-on insurance and warranties through caryard intermediaries.

Throughout this submission we will refer to the sale of add-on insurances and warranties as the sale of add-on products unless the discreet part of the submission requires us to differentiate.

The FBAA recognises previous findings by ASIC relating to poor consumer outcomes surrounding the sale of some insurance and warranty products. This is a result of a combination of:

- poor quality products;
- distorted remuneration models;
- products being sold by untrained people;
- failures to adequately assess a consumer's real needs before making recommendations;
- consumer behaviour (biases, lack of engagement, fatigue etc)

Poor sales practices and bad products have maligned a market that is an otherwise important part of consumers purchasing motor vehicles.

The FBAA's commitment is to work with ASIC to help identify rules and practices that ensure better consumer outcomes whilst recognising the validity of insurance and warranty products that provide consumers with important cover against unforeseen events. It is widely accepted that around 30% of consumers do not have sufficient reserves of savings to deal with unforeseen expenses and those relating to motor vehicle breakdowns or accidents are some of the most frequent encountered. ASIC's own Moneysmart website recognises that a working motor vehicle[1] is a high priority for consumers.

**General Position**

The FBAA does not support the concept of a deferred sales model in add-on products. We see such a model disadvantaging licensees and consumers. We believe it to be too fraught with logistical difficulties for administering such a model and it leaves consumers exposed. Without directly prohibiting the sale and financing add-on products, a deferred model ultimately frustrates the sale and financing of add-on products to a point where it is unlikely to occur. It has potential to exclude regulated entities from selling add-on products and driving sales practices towards unregulated entities. Reforms will be more effective where they address the specific problems of product quality and needs assessment rather than placing numerous barriers in place to make the sale unfeasible.

A deferred sales model fails to discriminate between genuine, quality products which need to be preserved and unnecessary, poor quality products which are the target of the mooted reforms.

Rather than a deferred sales model, we believe the focus must be on the quality of products and the correct assessment of consumer need prior to recommending a product. This could be supported by a number of integrity elements including:

- maximum limits based on a ratio of the value of the goods to the products acquired;
- monitoring payout ratios and maximum remuneration; and
- ASIC's ongoing monitoring of the quality of products being offered in the marketplace.

This submission will respond to the two proposals advanced by ASIC and also expands on the alternatives we consider may be more effective.

[1] https://www.moneysmart.gov.au/managing-your-money/saving/building-an-emergency-fund

**E1** We propose that the sale of add-on products by caryard 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) caryard 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.

Table 10 sets out key issues in the design of any deferred sales model.

Note: The proposed options in Table 10 are not intended to be definitive. We welcome further suggestions.

**E1Q1 Do you consider that it is appropriate to apply a deferral period to the sale of add-on products by caryard intermediaries?**

No. For the reasons provided elsewhere in this paper, we believe a deferral period will frustrate the sale of genuine products and leave consumers exposed to unmitigated risk.

**E1Q2 To what extent would a deferral address the consumer harms identified in this market?**

We understand the thinking behind a deferral is to act as a circuit breaker between the consumer's purchase of a motor vehicle and the decision to purchase add-on products. This follows observations made by ASIC in earlier work on the consumer's decision-making capabilities at the point of sale[2].

We do not endorse practices that exploit poor decision making by consumers however we do not agree that industry should be burdened with additional obligations that are aimed at changing consumer behaviour and preventing consumers acquiring inappropriate products.

[2] Report 470: Buying add-on insurance in car yards: Why it can be hard to say no - February 2016
Report 471: The sale of life insurance through car dealers: Taking consumers for a ride - February 2016

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Consumers are not harmed by selecting appropriate insurance or warranty products or by financing them under their finance contract. They are harmed by acquiring poor value products, products they do not need and through paying inflated prices. They are also harmed by being uninsured or underinsured.

A deferral model may reduce the instances of consumers buying poor value, inappropriate products but it will also dramatically increase the risk of consumers being uninsured or underinsured.

Provided the products offered are genuine and a need has been identified, the sale of add-on insurances and warranties should be treated no differently to the sale of other motor vehicle accessories such as paint protection, window tinting, towbars or roof racks.

**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?**
The impacts of a deferral model would be very large. A deferral model would render the sale of add on products virtually impossible. Consumers have low levels of engagement with financial matters, including insurance. We believe it is very unlikely that consumers would independently seek out cover at a later stage and that a break in time between purchase of the motor vehicle and the follow up sale of add-on insurances would likely lead to large numbers of consumers being uninsured or underinsured. We suggest this outcome is no more desirable than the outcomes observed in ASIC's work of consumers purchasing too much insurance or the wrong types.

A deferral model would also make it impossible for the consumer to finance insurance and warranties under their finance contact. Financiers will already have drawn up the finance contract for the purchase of the motor vehicle. They would have to reissue or amend the finance contract at a later date to extend it to the purchase of add-on products. At a practical level, financiers are not going to do this because of the administrative and regulatory burdens of doing this.

The impact will be significant for large and small business however the impact will be larger on smaller businesses as it will erode their margins and income streams and they do not have the scale to be able to operate profitably on reduced margins.

**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?**

We do not believe that the type of market, new or used car market, is relevant to the key points in discussion for the model under which the sale of add-on products can be allowed. The focus must stay on the quality products and the needs assessment. The rules must be the same for all. Clearly issues such as selling extended warranties on products which are already covered by statutory or manufacturer warranties may be more relevant to newer or new vehicles however we do not embrace an approach which attempts to differentiate between products and apply rules differently.

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

Price will be the obvious primary determinant from a consumer perspective. Insurance and warranty products can have an unlimited number of variations and exclusions between products and ASIC's own research demonstrates that consumers do not engage with the detail of various products enough to be able to make fully informed decisions.

It is usually a condition of a finance contract that the consumer purchase comprehensive car insurance over a financed vehicle. Consumers are already aware of the extensive comprehensive insurance market through advertising of the major brands and comparison services.

Dealer sales of comprehensive insurance has low levels of penetration because of the level of competition, consumer awareness and low rates of commission paid on sale of such products. In addition to comprehensive insurance being a requirement for financed vehicles, most consumers can understand the benefit of comprehensive insurance. This is a market that is working efficiently.

The markets for other add-on products is not as efficient for reasons including their niche positioning, limited number of product issuers and the value proposition for the consumer. Improving product quality, issuer accountability and consumer education may assist.

We believe consumers are most unlikely to be motivated to go online days after the purchase of their vehicle to purchase add-on products.

Your Choice, Your Voice

Many consumers find insurances and warranties generally uninteresting so they are not motivated to separately research them – regardless of their importance. For the most part, they are not likely to engage with the detail any more than they do now at the point of sale. Coupled with the fact that they will not be able to finance these products if purchasing them at a later stage, the result will be that the purchase of add-on insurances and warranties will be unlikely to happen in most cases if it happens later than at point of sale.

Consequently a deferral model will lead to consumers having significantly less insurance cover regardless of whether they need it or not.

**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?**
Absolutely. The objectives of the model are to ensure consumers do not acquire poor quality products that provide them with little to no benefit or pay exploitative prices.

A more effective way to achieve this outcome is to address other areas:
1. Needs Assessment
2. Product Design
3. Financing
4. Qualified people recommending the right products
5. Identify how the consumer can be better protected using wider ranging products and leveraged through their superannuation – including but not only income protection insurance that is deductible.

**Needs Assessment**
Require anyone recommending insurance or warranty products to consumers to conduct a needs assessment to demonstrate there is a genuine need for the products recommended. A needs assessment must also take into account any existing insurances and statutory warranties the consumer has. This would address issues such as the sale of GAP insurance to consumers where there is no gap and warranties where consumers already have statutory warranties.

The needs assessment should also include an affordability assessment which requires the discussion of add-on products to be held earlier in the sales process. This would address the problems associated with selling add-on products at delivery.

**Product Design**
Require product issuers to create genuine products that insure a genuine need, that do not overlap other insurances already taken out or available and are priced fairly according to the likelihood of a claim. The products must be clearly explained.

An example of this is gap insurance which should only be available to a consumer where a gap has been identified. The pricing of the insurance should be reasonable and the duration of the policy should be capped or tailored around the period for which a gap is expected to exist.

We also support consumers being afforded a cooling off period. This is a superior result to a deferred model that leaves consumers uninsured for a period.

**Financing**
It is possible to impose a maximum limit of add-on products that can be recommended or financed. For example, financiers could be required to fund add-on products to no more than a set percentage of the purchase price of the vehicle.

**Qualified people recommending the products**
Any staff member recommending add-on products should be an employee or representative of a licensee.

**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?**
Based on our desire to see a more effective solution than a deferred sales model we do not provide a detailed response to this question.

**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?**
The positioning of this question supports our view that a goal of the proposed model is to improve consumer understanding / engagement. A model as potentially harmful as the one proposed is not a suitable mechanism by which to do this.

Add-on insurances and warranties are not easy products to promote. Consumers will always have diminished levels of engagement with the detail of these types of products because, for most consumers, they are not interesting products. In that regard we believe paragraph 100 of CP294 omits one of the most important factors that inhibit consumer understanding of add-on products.

While all of industry would like consumers to engage better with the detail of these products and the implications of their purchase and financing, the notion is aspirational.

Our preference is to focus on product quality and correct cover so that consumers, regardless of their level of engagement, end up with appropriate and affordable cover.

Very few consumers will go away post-purchase of a motor vehicle and devote significant time to researching insurance and warranty products. They are more likely to do so if they have already purchased products and have a cooling off period within which to read their product disclosure material, conduct online research and price comparisons.

**E1Q9 Should a consumer opt-out mechanism be included?**
We are cautious about an opt-out mechanism. Consumers who are not making good decisions about the products they acquire are no more likely to make good, informed decisions about opting in or out. We believe a cooling off period is more effective.

**Commencement of the deferral period**

**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:

receives a consumer communication (with mandated content);

finalises the vehicle purchase and receives the consumer communication; or

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)?

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**E1.1Q2 Which sales sequence (see Figure 1) is most likely to meet our stated objectives and why?**
Sales sequence A is the only feasible order of events. A consumer cannot choose products before a vehicle which renders sequence C impractical. Financiers will not routinely revise credit contracts to accommodate the later purchase and finance of add-on products thus we do not believe sequence B will be practical.

Sales sequence A correctly orders car purchase, add-on products and then finance. It is incumbent on motor vehicle dealers and the sales processes they use, together with consumer participation to ensure the sales process is not unnecessarily complex, long or fatiguing. Including a mandatory cooling off period will allow consumers who acquiesce and purchase add-on products they don't need to bring an end to the sales spiel to reflect and cancel their policies at a later time.

**E1.1Q3 How could the point at which the deferral period commences be easily documented to be readily verified by all relevant parties?**
We do not support a deferral period. We strongly oppose any further disclosure-based solutions. The amount of mandated disclosure and paperwork already involved in NCCP transactions is overwhelming, (this is before factoring in other paperwork that forms part of the motor vehicle purchase). Adding further requirements will increase red tape, increase regulatory burdens and diminish the impact of existing disclosure documents.

**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?**
We believe this is highly unlikely to be accepted by any insurer. Alternately the cost is likely to be prohibitive.

### Duration of the deferral period

**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.



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

For reasons provided above we do not believe a deferral period operates in the interests of licensees or consumers.

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

**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?**

**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?**

### Consumer communication

**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?**

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

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

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

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**FBAA Response to E1.3 Q1-5**
We strongly oppose any recommendation for providers to have to provide additional disclosure to consumers relating to behavioural economics and consumer biases. It is not the provider's role to provide such information. Consumers already receive a large amount of information and disclosure relating not only to NCCP Act disclosure but also to elements of the motor vehicle purchase including ongoing servicing, user manuals and the like.

There is ample information available to consumers, including on the Moneysmart website should they be inclined to seek it out. We cannot envisage a scenario where it is possible to provide a consumer with even more information over and above all of the current NCCP disclosure together with motor vehicle documentation in circumstances where they will have capacity to read it, understand it and act on it. We recognise the benefits of clear consumer communication however do not believe this is the format under which further information should be provided to the consumer. A targeted needs analysis and good quality products provides a much greater consumer safety net.

No industry is "required to inform consumers about the availability of other products that provide similar [anything], but may be cheaper". This is uncommercial and anti-competitive. We oppose this on the strongest of grounds.

### Mechanical breakdown insurance and warranties

**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?**
Providers must be required to assess and document the consumer's need for such products. Any recommendation of duplicitous cover will be of itself unsuitable.

We would support a model where dealers provide the consumer with a choice of providers and not only offer a single supplier product on a 'take-it-or-leave-it' basis.

Product issuers must not design products to create gaps that require the consumer to purchase additional products.

Providers could create a customer record to contact the client when they are approaching the end of any statutory warranty period to follow up their insurance/warranty needs.

**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?**

We support changes that mandate a written needs assessment to be undertaken before recommending any products. That assessment will need to demonstrate that the recommended products are suitable for the consumer in that they:

a) do not already have this cover under other policies or statute; and
b) addresses a specific risk/need.

We also support requiring issuers to disclose approximate claim percentages/payout figures in the form of a statement to the consumer along the lines of "15% of people who take out this cover end up making a claim on it".

**E2Q2 What risk indicators could be introduced to improve the capacity of providers to monitor their representatives?**

Providers can monitor sales data to identify potential issues. Providers could consider data such as:

- Total add-on product sales as a percentage of total sales volume;
- Percentage of consumers who purchase add-on products

We also recommend monitoring with the view to removing any "soft dollar" and "volume bonus" income streams that are paid to dealer groups by insurers and are based on overall volume of products sold. Payments can amount to millions of dollars.

Coupled with monitoring of needs assessments this would provide a robust framework of monitoring.

**E2Q3 What sanctions would be most effective in deterring representatives from engaging in unfair practices at the point of sale?**
Forfeiture of remuneration, termination of licence, cancellation of ability to recommend add-on products, reporting to ASIC with enforcement action possible.

Thank you for inviting the FBAA to lodge this submission.

Yours faithfully

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Advisory Board Member – Small Business Association of Australia (SBAA)