



**ASIC**

Australian Securities & Investments Commission

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## Regulatory update to the general insurance industry

*A speech by Peter Kell, Deputy Chair,  
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*Insurance Council of Australia Annual Forum 2018 (Sydney, Australia)  
7 March 2018*

### **CHECK AGAINST DELIVERY**

#### **Introduction**

Thank you to the Insurance Council of Australia (ICA) for inviting me to present to you today.

I have three main topics I would like to talk about today:

- First, I want to talk about the environment we are currently in and the reforms currently underway in the financial services sector.
- Second, I will talk about the review of the General Insurance Code of Practice, including some of the changes ASIC has called for.
- Third, I will discuss some of ASIC's key areas of focus for general insurance in 2018.

#### **The current environment**

As you know, the broad financial services sector continues to experience a very high degree of media, regulator and public attention. There have been numerous examples of conduct that has failed to meet community expectations.

The establishment of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Sector is the most prominent example. The Royal Commission, under its terms, will focus on misconduct, as well as practices falling 'below community standards and expectations'.

Insurance is very much part of this picture. The life insurance sector is under unprecedented scrutiny across all channels. Your sector, general insurance, is also the subject of significant interest.

The current climate serves to emphasise that it has never been more important to put the consumer at the heart of everything that you do as a business. Further, the days of narrowly focusing on the minimal requirements needed to meet the ‘black letter of the law’ are over.

As an industry, you have probably become used to heightened community and media focus. The pace of regulatory change is unlikely to abate over the short to medium term.

While the Royal Commission is a major focus, the Government has committed to progressing previously foreshadowed reforms. ASIC welcomes this commitment, and we anticipate that the regulatory framework will have been strengthened by the end of this year.

This includes the introduction of a product intervention power for ASIC, and product design and distribution obligations on financial services sector participants.

The draft proposals indicate that issuers of financial products, including general insurers, will be obliged to:

- identify an appropriate target market for their products
- consider whether the product meets the needs of those individuals and is capable of being understood by them
- select distribution channels that are likely to deliver the products into the hands of individuals in the target market.

We have also recently seen significant steps in the area of complaints handling and dispute resolution, and I’ll discuss these in more detail later in my talk. This includes the establishment a single dispute resolution service, the Australian Financial Complaints Authority.

The Government has also signalled that it wishes to consider reforms to the exemption of insurance claims handling from the financial services conduct provisions of the Corporations Act, but will wait until the Royal Commission is concluded before taking final steps on this issue.

Additionally, the Government will also consult on extending the unfair contract term provisions in the ASIC Act to contracts of insurance.

In relation to ASIC’s powers, the work of the ASIC Enforcement Review Taskforce is preparing its final report to Government – examining a range of components of ASIC’s regulatory toolkit, including ASIC’s regulatory powers, the type and level of penalties available to ASIC, and the effectiveness of codes of conduct and self-regulatory initiatives in relevant industries.

There is a lot to digest in these ongoing reviews and reforms. But, importantly, as an industry you have created an opportunity to ensure the general insurance sector emerges from 2018 in a stronger position that it began. I’m referring here in particular to the opportunities arising from the review of the General Insurance Code of Practice (the Code) initiated by the ICA last year.

## General Insurance Code of Practice

I acknowledge the industry's proactive decision to initiate this review, with broad terms of reference, and the importance of the decision to incorporate independent oversight of the review.

The Code review presents the industry with an opportunity to demonstrate to the community that you have heard their concerns and are committed to addressing them, and will do so in a timely way.

For this to occur there must be a recognition and willingness among Code subscribers that the bar needs to be raised. I encourage the industry to fully embrace this opportunity to drive change and instil a positive corporate culture that places the consumer at the centre.

ASIC firmly believes that codes of practice, properly formulated and enforced, can help promote trust and confidence in the financial services sector. We welcome the review and the opportunity to contribute to it.

It is pleasing to see that a number of the suggestions we made in our submission to the review are discussed in the review's interim report, published in November 2017. That report seeks feedback on whether and how to implement some of the potential changes. I would therefore like to take this opportunity to highlight some of the changes we have suggested, which we think are most important to the success of the Code.

### Vulnerable consumers

ASIC welcomes the emphasis placed in the interim report on meeting the needs of vulnerable and disadvantaged consumers. After all, the risks and losses covered by general insurance policies can have a particularly devastating impact on financially vulnerable consumers, and it is therefore important to consider how their needs can be taken into account in designing and distributing insurance.

One of the learnings from ASIC's work in this area is that consumer vulnerability can change over time, and quite suddenly. We increasingly understand vulnerability as both individual and situational, meaning that when circumstances change, just about anyone can find themselves in a vulnerable situation. We encourage the insurance industry to consider the range of risk factors that may indicate vulnerability.

Vulnerable consumers will require additional assistance with many of their interactions with insurance products and providers, including during:

- the initial sales conversation
- policy renewal
- claims lodgement
- when making complaints – in particular, through the dispute resolution process.

It is encouraging that industry is considering a requirement that staff be trained to identify vulnerable consumers. Waiting for your customers to tell you that they are vulnerable

risks missing the many consumers who may not fully understand the particular financial problems they face; they may be reluctant to ask for help.

I suggest that you consider how the Code and your support of vulnerable consumers can best evolve to reflect the improvements in our understanding of financial vulnerability.

### **Enabling consumers to more readily compare products and assess value**

Our submission to the Code review noted that consumers are often faced with broad and varying definitions in general insurance policies. This can make it difficult for them to understand the extent of cover offered and to compare policies.

In our research into home insurance policies, we found that many consumers did not know that home insurance policies differed between insurers. They were unaware that policies can differ in their caps, limits and definitions of 'covered events'. I note that the ICA will lead work aimed at enhancing product comparability.

I suggest that, as part of this work, the ICA also consider how to better enable consumers to assess and compare product value. For example, consumers may need help to understand that there is typically a trade-off between price and coverage.

### **Investigation and surveillance practices**

The interim report also proposes a set of investigation and interview standards for possible inclusion in the Code.

ASIC has a close interest in these matters, having commenced a review of fraud investigation and surveillance practices by general insurers. This work stems from our concerns about reports of inappropriate practices by insurance investigators.

We certainly recognise the need for insurers to confirm the facts of a claim and ensure that only valid claims are paid. This ultimately reduces costs for all legitimate claimants. But insurers also need to ensure that the risk of consumer detriment caused by fraud investigation techniques does not lead to poor outcomes and inappropriate decisions around claims.

As part of our review of fraud investigation and surveillance practices, we will shortly convene a stakeholder workshop with consumer and industry representatives. The workshop will provide an opportunity for stakeholders to be heard on appropriate investigation practices. It will provide a mechanism to develop solutions to address investigation practices that might also cause claimants to withdraw valid claims. The aim is to allow appropriate investigations while preventing unnecessary consumer harms.

It may be that the consumer harms can be addressed, at least in part, through a further strengthening of the principles for the conduct of fraud investigations proposed to be included in the Code.

We look forward to working with the industry further on this issue as our work progresses.

## Standards for third-party product distributors and outsourced service providers

The Code review has also signalled the need for insurers to take greater responsibility for the conduct of third-party product distributors and outsourced service providers.

For example, the interim report raises the problem of poor conduct by distributors, and suggests that relevant agreements with insurers could incorporate higher expectations around conduct. This is a positive proposal, but we consider that the industry could take this further.

Insurers should set explicit standards in such agreements of what behaviour is and is not acceptable. And they should put processes in place so that they can satisfy themselves that high standards are being adhered to, and the treatment of customers is as they would expect.

Here it is important to think about community expectations around insurer responsibility for the products they underwrite and issue when developing industry standards.

In our work we have seen several examples of poor accountability by insurers for the distribution of their products to the end consumer. One glaring example, where ASIC has taken significant action in the last 12 months, is in the area of add-on insurance sold in car yards. Insurers cannot walk away from how their products are distributed, regardless of the technical legal position. Consumers expect the underlying insurer to be aware of the outcomes that the products they underwrite have for consumers, however they are sold.

Ultimately, the quality, scope and ambition of the Code will determine in large measure the extent to which industry practice meets consumer needs and expectations. I therefore urge you to seize this opportunity to make the Code as strong as it can possibly be.

## Code approval by ASIC

A further important aspect of the review of the Code is whether to seek approval from ASIC, under the long-standing code approval standards that ASIC sets out in [Regulatory Guide 183 Approval of financial services sector codes of conduct](#) (RG 183).

Whether or not you seek approval of your updated code is a matter for the industry. But having said this, the message I have for you today is that the insurance code is a good code, an important code, and we think it is capable of meeting ASIC's approval requirements.

We believe that ASIC approval would assist to strengthen consumer confidence in the Code. Approval of the Code by ASIC provides an additional marker of the quality of the Code, having met the standards of our regulatory guidance.

I also note that the Treasury Enforcement Review's consultation paper on codes of conduct put the position that industry participants would be *required* to subscribe to a Code approved by ASIC, and explored issues around governance, enforceability and compliance monitoring mechanisms that could be associated with this regulatory model.

## Key areas of ASIC focus in 2018

I wanted to also provide you with a brief update of our ongoing work on add-on insurance sold with cars. The need for broad ASIC intervention and substantial refunds to consumers has demonstrated the risks for insurers in not placing consumers at the centre of product design and distribution.

### Add-on insurance sold through car yards

We continue to work to address unsustainable and unfair business models in the sale of add-on insurance sold through car yards. Our response includes developing a deferred sales period for these products.

We received over 20 submissions from insurers, lenders, car dealers and consumer groups in response to our [2017 consultation paper](#), demonstrating strong interest and engagement on the issue. ASIC is considering this issue carefully, particularly in relation to how a deferral period can improve consumer engagement and understanding of the products being sold to them.

We welcome industry's support for a deferred sales model. We are working with industry to develop the model and we intend to undertake a second round of consultations on a refined model. Doing so will enable us to test key aspects of the proposed model with you.

To date, remediation to consumers for past unfair sales of add-on insurance has totalled over \$120 million. This demonstrates that engaging in conduct that does not meet community standards and expectations can prove expensive for insurers.

We continue to work with individual insurers to agree on consumer remediation that responds to the consumer harm caused by past conduct. We expect that all insurers in this market will address the consequences of unfair practices, in relation to the design, sale and price of their products, through such programs.

I'll conclude on this issue by making an observation about the upcoming product design and distribution reforms. The work that was done by our joint working group with insurers, car dealers and consumer groups on developing design and distribution principles for add-on insurance should put the industry in a strong and positive position to develop appropriate approaches to complying with the new obligations. The industry's participation in that work demonstrates leadership and a commitment to change, and shows a positive approach to prioritising the needs and interests of consumers.

### Consumer credit insurance

ASIC also continues to focus closely on the sale of consumer credit insurance (CCI), given our concerns about miss-selling of this add-on product.

Similar to add-on insurance sold through car yards, we have found consumers being sold CCI:

- without their knowledge or consent

- when they were ineligible to claim against the unemployment or disability cover because they did not meet the employment criteria
- where they do not need cover – for example, the sale of life cover under CCI policies to young consumers with no dependants
- on top of all that, being overcharged for the product.

This pattern of mis-selling reinforced the need for us to review the past CCI sales practices of 11 lenders, to check compliance with our publicly stated recommendations for the sale of CCI. We will pursue remediation and regulatory action where this review uncovers poor conduct. The lessons from our broader add-on insurance work provide a clear statement to insurers of ASIC's views on when products have been sold to consumers who do not need them.

We also worked with relevant stakeholders last year to improve outcomes for consumers. As a result of that process, the banks have committed to a range of measures to improve sales practices, including a deferred-sales model for CCI sold with credit cards over the phone and in branches.

The sales deferral reduces the risk that a consumer will feel pressured to purchase the CCI product, or that they will purchase a CCI product that does not meet their needs. However, more can be done. I suggest that insurers review the value offered by their CCI products and act to improve product value. And that CCI only be offered to a target market that will benefit from it.

Further, insurers should move to implement similar changes to those being introduced for add-on insurance sold through car yards. Not doing so could be interpreted as a failure by the industry to apply lessons learnt more broadly.

## Dispute resolution

I would like to take this opportunity to say a few words about dispute resolution. While the current reforms are not just about general insurance, it is important for your sector.

As I noted earlier, the legislation to create the new Australian Financial Complaints Authority (AFCA) has now passed, and the process to move financial services dispute resolution to the new body has started. AFCA will start operations by 1 November this year. This will provide enhanced access to free, fast and binding dispute resolution for Australian consumers and small businesses.

As the Ramsay Review reiterated, fair, timely and effective dispute resolution is a cornerstone of the financial services consumer protection framework. The combination of firms' internal dispute resolution (IDR) procedures and access to a free, independent external dispute resolution (EDR) scheme currently provides redress for many tens of thousands of Australians each year. Strengthening these dispute resolution requirements will help deliver higher standards and better outcomes in the financial services market.

In this context I want to stress the importance of insurers maintaining IDR systems and staff that are adequately resourced. In any business, this area should have appropriate authorisation within the organisation to resolve disputes quickly and efficiently for consumers.

The Code governance committee's recent report of a 73% increase in claims-related breaches of the Code last year is a timely reminder in this regard. I appreciate that the general insurance industry has the difficult task of assessing large volumes of insurance claims following, in particular, natural disasters. But insurers' claims management must be scalable to cope with a spike in claims. The committee's report demonstrates further improvements are needed.

Insurers should also be analysing this dispute data to learn about where the issues are, and act to make changes to customer friction points: whether it's in product design, sales practices, or claims handling.

A significant portion of disputes at the Financial Ombudsman Service are resolved by agreement. As a business, you should consider whether better IDR would help reduce the costs for you and your customers in resolving disputes at EDR.

As you will have seen, we have started the [public consultation process on reviewing our Regulatory Guide 139](#), relating to approval and oversight of EDR schemes, so that we can update it for the establishment of AFCA. We have started this process as we believe that clarity about ASIC's policy approach at this stage of the transition will assist all stakeholders.

Our guidance will be finalised to coincide with the commencement of AFCA – by 1 November this year.

We will also publicly consult on new IDR standards and the mandatory, firm-level IDR reporting requirements that are also set out in the AFCA legislation. This data collection will identify firms and will help improve transparency and accountability of firms' IDR practices. We will start our consultation on this component, after AFCA commences its operations.

## Conclusion

In conclusion, as you can see, there is clearly a lot of activity in your sector! This means that the ongoing dialogue and relationship we have with both individual insurers and the industry body is very important. I'd like to again thank the ICA for their productive engagement on many of the issues I've mentioned today.

I look forward to working collaboratively with you over 2018 to ensure that your industry, one that is very important for Australian consumers, remains healthy and continues to meet evolving community expectations.