

24 August 2018

By email: UCTinsurance@treasury.gov.au

Manager, Insurance and Financial Services Unit
Financial System Division
The Treasury
Langton Crescent
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Dear Sir/Madam

Submission: Extending unfair contract terms protections to insurance contracts

Thank you for the opportunity to comment on Treasury's proposal to extend unfair contract terms (**UCT**) protections to insurance contracts.

The case for extending UCT laws to insurance contracts is clear.

The insurance industry is virtually the only industry enjoying an exemption from the economy-wide UCT regime. There is clear evidence that this loophole should be closed. Public scandals in life insurance and add-on insurance, as well as the experiences of many people who Consumer Action has assisted, all point to the need for the UCT regime to cover insurance. This reform has been recommended in three separate inquiries and reviews over the past year.

Consumer Action strongly supports many elements of Treasury's proposal. It strikes the right balance of fairness and captures many of the key issues experienced by consumers. The extension of the *Australian Securities & Investments Act (ASIC Act)* regime to insurers is a consistent and sound approach. We welcome key elements of the proposal, such as the meaning of unfair, the coverage of a broad range of standard form consumer contracts and the inclusion of third-party beneficiaries. We have also provided comment on where the regime should be strengthened. This includes applying the fairness test to excesses and ensuring an effective transition for life insurance contracts.

Our comments are detailed further below.



About Consumer Action

Consumer Action is an independent, not-for-profit consumer organisation with deep expertise in consumer and consumer credit laws, policy and direct knowledge of people's experience of modern markets. We work for a just marketplace, where people have power and business plays fair. We make life easier for people experiencing vulnerability and disadvantage in Australia, through financial counselling, legal advice, legal representation, policy work and campaigns. Based in Melbourne, our direct services assist Victorians and our advocacy supports a just market place for all Australians.

Summary of position

Our position on the key elements of Treasury's proposal is summarised in the table below.

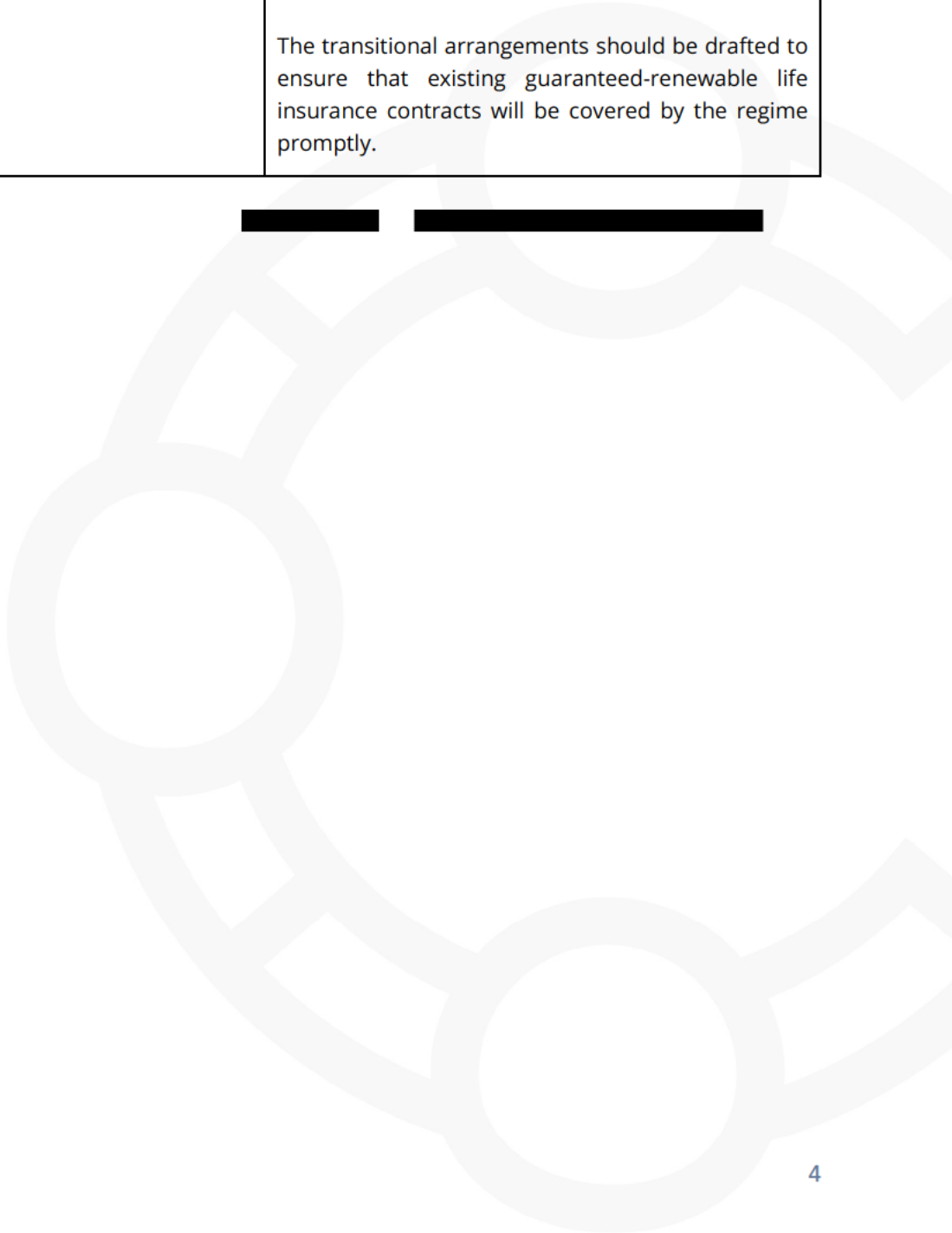
Treasury proposal	Consumer Action response
Applying the ASIC Act to insurance contracts	
Amending section 15 of the <i>Insurance Contracts Act 1984 (IC Act)</i> to allow the current unfair contract terms laws in the ASIC Act to apply to insurance contracts regulated by the IC Act.	Strongly support The existing ASIC Act provisions should apply to insurance contracts. The proposed reforms can be enacted through minor amendments to the IC Act and secondary materials.
Proposed tailoring of UCT laws for insurance contracts	
Main subject matter The 'main subject matter' of an insurance contract will be defined narrowly as terms that describe what is being insured, for example, a house, a person or a motor vehicle.	Strongly support The proposed definition of 'main subject-matter' is in line with existing unfair contract terms laws and insurance law.
Upfront Price Clarification will be provided that the 'upfront price' will include the premium and the excess payable and that these will not be subject to review.	Partly oppose The upfront price should be the upfront premium. The policy excess should not be considered part of the 'upfront price'. Excesses are not always transparent and exempting excesses will create a risk of regulatory arbitrage.
Standard form contracts	Strongly support We support the inclusion of standard form contracts with various coverage options.



Treasury proposal	Consumer Action response
<p>A contract will be considered as standard form even if the consumer or small business can choose from various options of policy coverage.</p>	
<p>Meaning of unfair</p> <p>When determining whether a term is unfair, a term will be reasonably necessary to protect the legitimate interests of an insurer if it reasonably reflects the underwriting risk accepted by the insurer in relation to the contract and it does not disproportionately or unreasonably disadvantage the insured.</p>	<p>Strongly support</p> <p>We support the proposed definition. The second limb would provide appropriate balance between the interests of insurers and their customers, and will be important for the regime to operate effectively.</p>
<p>Terms that may be considered unfair</p> <p>Examples specific to insurance will be added to the list of examples of kinds of terms that may be unfair, which could include terms that permit the insurer to pay a claim based on the cost of repair or replacement that may be achieved by the insurer, but could not be reasonably achieved by the policyholder.</p>	<p>Strongly support</p> <p>We support the inclusion of specific examples of unfair terms. The examples listed capture the most significant types of clauses.</p> <p>We have recommended additional examples which would address other problems we have seen.</p>
<p>Remedies for unfair terms</p> <p>Where a term is found to be unfair, as an alternative to the term being declared void, a court will be able to make other orders if it deems that more appropriate.</p>	<p>Support</p> <p>We support the Courts being able to make orders other than voiding a term. This will avoid inadvertently unfair outcomes for consumers.</p>
<p>Third-party beneficiaries</p> <p>The definition of 'consumer contract' and 'small business contract' will include contracts that are expressed to be for the benefit of an individual or small business, but who are not a party to the contract.</p>	<p>Strongly support</p> <p>We strongly support the inclusion of contract beneficiaries, including beneficiaries of group life insurance policies held in superannuation.</p>
<p>Tailoring for specific insurance contracts</p> <p>For life policies, as defined by the Life Insurance Act 1995, which are guaranteed renewable, it will be made clear that a term which provides a life insurer</p>	<p>Partially support</p> <p>We accept that life insurers should continue to be able to increase premiums under guaranteed renewable life insurance policies. However, insurers</p>



Treasury proposal	Consumer Action response
<p>with the ability to unilaterally increase premiums will not be considered unfair in circumstances in which the premium increase is within the limits and under the circumstances specified in the policy.</p>	<p>should justify and be transparent about such increases.</p>
<p>Transitional Arrangements</p>	<p>Partially support</p> <p>12 months is an adequate transition period, as insurers should be preparing for the extension of the UCT regime now.</p> <p>The transitional arrangements should be drafted to ensure that existing guaranteed-renewable life insurance contracts will be covered by the regime promptly.</p>



General comments

We congratulate Treasury on proposing very effective reforms to bring insurance into the UCT regime. We strongly support the vast majority of the proposal and the rationale outlined.

In our view, finally bringing insurance contracts within the UCT regime can deliver on a significant and desirable policy objective—a consistent UCT regime for standard form consumer and small business contracts in Australia. This will be a much-anticipated milestone in consumer protection regulation.

In 2008, the Productivity Commission stated:

[S]tatutory carve outs... potentially provide unscrupulous operators with opportunities to make minor changes to their activities so as to slip between the regulatory cracks. To avoid this, there should be no exclusions of particular sectors from the new national generic consumer law.¹

More recent reviews and inquiries have recommended extending the UCT regime to insurance, including

- the Australian Consumer Law Review in 2017 (**ACL Review**),²
- the Senate Economics References Committee Inquiry into the general insurance industry in 2017 (**Senate Committee Inquiry**),³ and
- the Parliamentary Joint Committee on Corporations and Financial Services inquiry into the life insurance industry (**Joint Parliamentary Committee Inquiry**).⁴

We note that the ACL Review and Senate Committee Inquiry recommendations have been accepted by Government. The Government's response to the Joint Parliamentary Committee recommendation is pending.

The Senate Committee Inquiry into general insurance stated:

General insurance plays an important role in maintaining the financial stability of consumers, and indeed, of the Australian economy. Given this, effective protections are essential during all stages of a consumer's relationship with an insurer. The committee is of the view that the exemption of general insurers from the unfair contract terms provisions... is unwarranted and creates a significant gap in consumer protections.⁵

The Parliamentary Joint Committee concurred, stating:

[P]ersistent misconduct by today's corporate life insurance industry demonstrates that the rationale for Section 15 of the Insurance Contracts Act is no longer credible. It is simply no longer reasonable to exempt the life insurance industry from the application of consumer protections.⁶

¹ Productivity Commission, *Review of Australia's Consumer Policy Framework*, April 2008, p. 24

² *Australian Consumer Law Review: Final Report*, March 2017, proposal 10, p 52.

³ Senate Economics References Committee, *Australia's general insurance industry: sapping consumers of the will to compare*, 10 August 2017, recommendation 11, p 65.

⁴ Parliamentary Joint Committee on Corporations and Financial Services, *Life Insurance Industry*, 27 March 2018, Recommendation Recommendation 3.1, p 50.

⁵ Senate Committee Inquiry, para 5.13.

⁶ Parliamentary Joint Committee Inquiry, para 3.83.



Significance for consumers

Consumer Action has advocated for these reforms because the exemption for insurers causes significant consumer harm. This is compounded by the fact that existing consumer protections for insurance do not provide adequate recourse.

Our report *DENIED: Levelling the playing field to make insurance fair*⁷ tells the stories of people who have experienced 'claim shock', when their insurers reject their claims in unexpected and unreasonable ways. This has occurred because some terms in insurance contracts are heavily-weighted in favour of the insurer, to the detriment of the insured person. Claim shock also occurs when policy wording is unclear and clauses are applied in unfair ways.

These experiences have caused a public trust deficit for insurers, which is highly problematic when trust is core business for insurers. Insurers have failed to justify their own contract terms and to tell their customers what their insurance products do, clearly and transparently.

The UCT regime should address these systemic problems and prevent people in vulnerable circumstances from facing the financial and personal stress of an unfairly denied insurance claim. It could make the insurer-customer relationship a healthier one, and play a key [REDACTED] [REDACTED]

Consistency

The overarching objective of these reforms should be to apply the existing unfair contract terms (**UCT**) regime under the ASIC Act to insurance contracts consistently with the existing regime. In our view, Treasury's proposals could be effectively implemented by amending the *Insurance Contracts Act 1984* (**IC Act**), without substantively amending the ASIC Act.

It is a relatively modest step to bring life and general insurance under the UCT regime. Private health insurance, government insurance and re-insurance are already bound by UCT laws. The laws as they stand are well-established and broad enough to apply effectively to a wide range of industries.

⁷ February 2018, <https://policy.consumeraction.org.au/2018/02/13/denied-levelling-the-playing-field-to-make-insurance-fair/>.



Applying the ASIC Act to insurance contracts

1. Do you support the proposal to amend section 15 of the IC Act to allow the current UCT laws in the ASIC Act to apply to insurance contracts regulated by the IC Act?

2. What are the advantages and disadvantages of this proposal?

We strongly support the approach outlined in the proposal paper. While there are various ways a UCT regime could apply to insurers, there are compelling reasons to bring insurers under the existing UCT laws.

This approach:

- provides more consistent consumer protections across financial services—relevant reviews have emphasised the importance of this,
- will lead to more consistent decisions in the Courts and the Australian Financial Complaints Authority (AFCA),
- future-proofs the regime, ensuring that any future reforms will apply to financial services across the board (for example, reforms to penalties), and
- does not create any disadvantages for consumers.

3. What costs will be incurred by insurers to comply with the proposed model to the extent possible, identify the magnitude of costs and a breakdown of categories (for example, substantive and/or administrative compliance costs in reviewing contracts).

The Productivity Commission reported in 2008:

[[I]n those countries and jurisdictions that have introduced new regulations, there is little evidence of significant compliance costs or other burdens for business (and therefore consumers). In fact, some businesses in Australia have supported such regulation, and many are used to complying with provisions against unfairness in industry codes.⁸

The key advantage of the UCT regime is that it has prompted a proactive approach to improving contracts across other industries. It has not led to expensive and protracted disputes.

In 2013, the Australia Competition and Consumer Commission (ACCC) reviewed unfair contract terms in airline, telecommunications, fitness, vehicle rental industries and some common online trader contracts. After the ACCC found that certain types of terms were unfair, 79 per cent of unfair terms were removed from standard form consumer contracts.⁹ When UCT laws were extended to standard form small business contracts, the Australian Securities and Investments Commission (ASIC) announced that the major banks reviewed their small business loan contracts and removed unfair contract terms.¹⁰ We expect the experience of other industries to be a strong indicator of what the insurance industry will need to do to comply.

⁸ Productivity Commission, 2008, p 35.

⁹ ACCC, *Unfair contract terms Industry review outcomes*, March 2013, p. 1.

¹⁰ ASIC, *17-278MR Big four banks change loan contracts to eliminate unfair contract terms*, 24 August 2017, <http://asic.gov.au/aboutasic/media-centre/find-a-media-release/2017-releases/17-278mr-big-four-banks-change->



We are keen for insurers to provide evidence of compliance costs, particularly any costs which are intended to be passed on to consumers, and the way in which these costs will be passed on. We would also expect insurers to take into account the potential for decreases in some types of consumer disputes when calculating their compliance costs.

**4. Do you support either of the other options for extending UCT protections to insurance contracts?
5. What are the advantages and disadvantages of these options?**

We do not support the other options for extending UCT protections. These approaches would contradict the important policy objective of consistent UCT regulation, and would be inaccessible and ineffective for consumers. We strongly caution against either of the alternative approaches outlined in the proposal paper.

Enhance existing IC Act remedies

Creating a new 'hybrid' regime under the *Insurance Contracts Act 1984 (IC Act)* would be contrary to the objective of consistent financial services regulation. It would also not be possible to establish a logical and effective regime which merges the UCT regime with the duty of utmost good faith (**DUGF**). The two are conceptually distinct.

The UCT regime is preventative and systemic in effect. The requirements and test are clearly set out in legislation. The regime addresses the power imbalance between a company that offers goods or services under contracts offered on a 'take it or leave it' basis, and their customers who rely on those goods and services. Since its introduction in 2010, it has improved standard form consumer contracts across other industries (as outlined in the response to question 3 above).

Conversely, the DUGF is an indistinct mutual duty at common law, defined in Court authority rather than in legislation. This makes it difficult for a non-lawyer to know about or understand the DUGF. It provides an individual right to litigate, which is practically inaccessible to anyone who is not a specialist lawyer. National Legal Aid has reported that the DUGF is rarely invoked by people in their disputes with insurers.¹¹

As the Parliamentary Joint Committee stated:

[T]he symmetrical nature of the good faith duty is incompatible with the highly asymmetrical nature of the relationship between an individual or small business dealing with large powerful life insurance companies'.

The committee notes that in the early 1980s with an industry dominated by mutual life insurers, it may have been possible to sustain an argument that a duty to act in good faith may have been sufficient to offset the loss of substantial consumer protections through the application of section 15 of the Insurance Contracts Act.

loancontracts-to-eliminate-unfair-terms/.

¹¹ National Legal Aid, *Submission to Senate Economics Legislation Committee Inquiry into the Trade Practices Amendment (Australian Consumer Law) Bill*, 14 August 2009, p 4.



However, persistent misconduct by today's corporate life insurance industry demonstrates that the rationale for Section 15 of the Insurance Contracts Act is no longer credible. It is simply no longer reasonable to exempt the life insurance industry from the application of consumer protections.¹²

Over more than three decades of operation, the DUGF has not proven itself to be an effective consumer protection. On the contrary, it has been used to great effect by insurers to deny claims.

Consumer Action reviewed 147 Financial Ombudsman Service (**FOS**) determinations over more than four years in which a breach of the DUGF was argued by the insurer, customer or both. We found that:

- in 83% of cases, the insurer argued the insured person had breached the DUGF through fraud, misleading or untruthful conduct or statements, non-disclosure or non-cooperation,
- FOS found in favour of the insured person in 38 per cent of cases,
- in only three cases, FOS found the insurer breached the DUGF. Consumers often mistakenly thought that under-insurance or 'unexpected' exclusions were a breach of the DUGF,
- in 66 per cent of cases, FOS found there was no breach of the DUGF. Our view is that this points to the DUGF being over-used by insurers in an attempt to deny claims. It is also not providing effective recourse in common consumer complaints.

The vast majority of insurance consumer disputes are determined through external dispute resolution (**EDR**). The DUGF has not provided 'fair' systemic outcomes for consumers about inappropriate or unexpected insurance policies through FOS.

Since 2013, ASIC has had the power to pursue an insurer for breach of the DUGF in handling claims or potential claims.¹³ However, to our knowledge, ASIC has not used this power. If ASIC did use this power, it may not provide a better remedy or outcome than an action for unconscionable conduct.¹⁴

Regarding the specific elements of the possible changes outlined at page 12 of the proposal paper:

- The continued operation of section 15 of the IC Act to exclude ASIC Act protections is clearly out of step with the objectives of consistency and fairness in financial services regulation. Section 15 leaves 'an enormous gap in consumer protections'.¹⁵
- A tailored definition of 'unfair contract term' within the IC Act is unnecessary. The existing definition in the ASIC Act operates effectively for every other standard form consumer contract.
- A breach of the DUGF and non-reliance on the term is a much less effective remedy for consumers than the UCT regime could provide.
- A new and novel model would create significant uncertainty for insurers and is highly unlikely to be understandable and accessible for consumers. Most individual consumers would have no chance of successfully understanding and arguing a proposed hybrid cause of action along these lines. Clarity and accessibility are important elements of the UCT regime, and this must be maintained when insurers are brought under the regime.
- It is unclear how the jurisprudence of the UCT regime and DUGF would apply to a hybrid regime. This is a conceptually jarring and unclear approach.

¹² Parliamentary Joint Committee Inquiry, paras 3.81-3.83.

¹³ IC Act section 14A.

¹⁴ Under Part 2, Division 2, Subdivision C of the ASIC Act.

¹⁵ Parliamentary Joint Committee Inquiry, para 3.80.



Reforming the existing DUGF regime and continuing to rely on the IC Act to protect consumers would simply reinforce the complexity and inaccessibility of consumer protections under the IC Act.

Anh's story

Anh (not her real name) took out consumer credit insurance (**CCI**) with her mortgage in 2012. She worked in the same job for seven years but was made redundant in 2017. She started a new job approximately one month later.

After around 83 days, she became unable to work due to mental illness and was hospitalised. She made a claim under her CCI policy.

The insurer declined the claim, relying on a policy clause which stated that that the insurer will only pay a benefit if the insured was 'employed for at least 90 consecutive days immediately before' becoming disabled.

The insurer has not paid Anh's claim. Consumer Action is assisting Anh.

In Anh's case:

- The insurer narrowly applied the 90-day requirement, not taking into account the time Anh was paid for annual leave and public holidays.
- The insurer's reading of the DUGF requirement to act consistently with commercial standards of fairness and decency and have due regard to the interests of the insured¹⁶ did not lead to the claim being accepted. It reflects an outdated view of the commercial realities of the workforce, as work has become increasingly casualised and continuity of employment over years is becoming less common.
- The General Insurance Code of Practice requirement to conduct claims handling in an honest, fair and transparent manner¹⁷ also did not lead the insurer to accept the claim.

Anh could have made a claim for involuntary unemployment when she was made redundant, but only if she had not returned to work so quickly. The insurer denied her subsequent claim without consideration of her long-term stable employment.

It is clear that the DUGF does not protect people in circumstances where a broad condition is applied harshly to people when they make a claim.

Introduce the existing UCT laws into the IC Act

Similar to a hybrid UCT-DUGF model, a 'tailored' UCT regime in the IC Act does not accord with the broad objective of consistency in financial services consumer protections.

While this approach may not lead to the same complexities, risks and inefficacies as a hybrid UCT-DUGF model, it is also less likely to deliver consistent outcomes for consumers across different financial products and

¹⁶ *AMP Financial Planning Pty Ltd v CGU Insurance Ltd* (2005) 146 FCR 447.

¹⁷ General Insurance Code of Practice section 7.2.



services. Extending the ASIC Act UCT regime to insurance avoids the complications and uncertainties of creating a new UCT regime within the IC Act.

6. What costs would be incurred by insurers to comply with these options? To the extent possible please identify the magnitude of costs and a breakdown of categories (for example, substantive and/or administrative compliance costs).

See our response to question 3 above.

Proposed tailoring of UCT laws for insurance contracts

These reforms could be implemented by including specifics of the proposal in the Explanatory Memorandum (EM) to the amending Bill, ASIC guidance and AFCA approach documents. This would be consistent with how UCT laws were implemented for every other industry. Clear objectives in the EM and tailored guidance for insurance will be important to implement these reforms in line with the broader aims of the UCT regime.

Terms excluded from the UCT laws

[REDACTED]

Main Subject Matter

The meaning of 'main subject matter' in relation to insurance contracts will be a critical element in the effectiveness of these UCT reforms. This definition will play a key part in determining:

- the extent to which the insurance industry reviews and improves its contract terms, and
- the effectiveness of the regime for a person who pursues a dispute against an insurer on the basis of an unfair term in the contract.

We note again that the meaning of particular elements of the UCT regime for insurance contracts can be defined in the EM and guidance, as has been the case for every other type of contract under the existing regime. Our comments should be read in that light.

7. Do you consider that a tailored 'main subject matter' exclusion is necessary?

8. If yes, do you support this proposal or should an alternative definition be considered?

We strongly support the proposed definition of 'main subject matter' as it relates to insurance. This is a sound approach, in line with the definition under existing insurance laws and the intention of the current UCT regime.

A clear definition of 'main subject matter' is obviously important for clarity, effectiveness and consistency with the existing regime. Insurance law already defines 'subject matter', and further guidance could be provided in the EM and by ASIC.



Under the IC Act, the 'subject-matter' of an insurance contract is the thing being insured, such as 'property' or a 'road motor vehicle'.¹⁸ It could also be a person or group of people.¹⁹ Importantly, the subject-matter of an insurance contract is distinct from the insured event and risk (or cause of loss) under the contract.²⁰

A precise definition of 'main subject matter', which is consistent with insurance law, means the fairness test will apply across a broad range of contracts terms. This is integral to the effective operation of the regime. Conversely, if the 'main subject matter' definition was broadened so that the UCT regime had similar application to New Zealand's laws, we would expect the regime to be ineffective.

9. Should tailoring specific to either general or life insurance contracts also be considered?

There is no evidence that the definition should be tailored for general or life insurance contracts.

Upfront Price

10. Do you support this proposal or should an alternative proposal be considered?

11. Do you agree that the quantum of the excess payable under an insurance contract should be considered part of the upfront price and, therefore, [REDACTED] from [REDACTED]

We support the upfront price of an insurance contract being defined as the upfront premium paid.²¹ We do not support the quantum of the premium being excluded from review under the UCT regime.

The quantum of the policy excess must be reviewable under the regime, for the following reasons:

- The total excess payable, even under a basic, mainstream insurance contract, can be very difficult for a consumer to know upfront. Different types of excesses can apply to different types of claims. Insurers may not be transparent about the application and quantum of various excesses.
- The 'basic' or 'standard' excess under a policy is often clearer than other types of excesses. This can mislead people into thinking the basic excess amount is the only amount payable if they make a claim.
- It is difficult to distinguish terms which are about the *application* of an excess from terms which are about the *quantum* of that excess. This is particularly true because there are wide variations in policy wording between insurers. It would be difficult to determine if a term relating to an excess is reviewable or not. This complexity would make it very hard for individual consumers to understand and access the UCT regime if they wished to pursue a dispute about an excess.
- Carving out the quantum of excess(es) creates a risk of regulatory arbitrage for commercial gain. For example, an unscrupulous insurer could charge low premiums to gain and retain customers, while imposing very high excesses on claimants to maintain its profitability. This could cause significant financial and personal distress to claimants in very vulnerable circumstances, but would not breach UCT laws if the quantum of excess was excluded.

¹⁸ IC Act sections 17, 44, 49 and 65.

¹⁹ Such as workers under a workers' compensation policy: *Wallaby Grip Ltd v QBE Insurance (Australia) Ltd* [2010] HCA 9, para 29 (*Wallaby Grip*).

²⁰ *Wallaby Grip* at para 29 per French CJ, Gummow, Hayne, Heydon, Kiefel JJ citing Professor Malcolm Clarke.

²¹ Under the ASIC Act section 12BI(2).



Transparency of excesses

Insurers currently take varied approaches to disclosing their excesses. Some are much more transparent than others. Some are more 'expected' by customers than others.

Travel insurance excess clause

EXCESS

Your standard excess is shown on your Certificate of Insurance and applies EXCEPT where a benefit is payable under the following sections:

Section 1.1 OVERSEAS EMERGENCY MEDICAL ASSISTANCE

Section 1.5 HOSPITAL CASH ALLOWANCE

Section 4.2 LUGGAGE & PERSONAL EFFECTS DELAY EXPENSES

Section 4.4 THEFT OF CASH

Section 7.9 CABIN CONFINEMENT

Section 7.12 FORMAL CRUISE ATTIRE DELAYED

Section 7.13 MARINE RESCUE DIVERSION

In some circumstances we may impose an additional excess for claims arising from some medical conditions. We will inform you in writing if any additional excess applies.

If you purchase ADVENTURE PACK or SNOW PACK the following sections have a \$500 excess which applies to all claims under those sections (in addition to any standard excess) if your claim arises from your participation in sports and activities listed under ADVENTURE PACK in the ADDITIONAL OPTIONS section, or your participation in snow sport activities:

Section 1.2 OVERSEAS EMERGENCY MEDICAL & HOSPITAL EXPENSES when ADVENTURE PACK or SNOW PACK has been purchased

Section 2.1 CANCELLATION FEES & LOST DEPOSITS when ADVENTURE PACK or SNOW PACK has been purchased (emphasis added)

Allianz, Travel Insurance Product Disclosure Statement (including Policy Wording), 10 February 2017, p 17.

In this example, the Product Disclosure Statement (**PDS**) only discloses the quantum of the basic, 'adventure pack' and 'snow pack' excesses. The clause indicates that additional excesses may be payable but does not specify the amount of any additional excess(es).

Under this PDS, it is unclear:

- if or how the insured can find out the quantum of excesses payable under certain sections (for example, whether these amounts are in the certificate of insurance), and
- when the insurer will inform the insured in writing of any additional excess payable.

In contract terms such as this, it is difficult to separate the quantum of the excesses from other terms relating to the excesses, particularly where only part of the total excess is transparently disclosed. Hidden or uncertain excesses can mislead people as to the total quantum, as they may believe that the clearly disclosed standard or basic excess is the total excess.



It would be contrary to the intention of the UCT regime to define any element of excesses as part of the 'upfront price' of an insurance contract. This is particularly the case where:

- the application and quantum of the excess is not transparently disclosed to the consumer at the time the contract is entered into,
- it is unclear whether the insurer is able to inform the customer of the quantum of the excesses at the time of entering into the contract, and
- the quantum of the excesses will depend on the circumstances in which the consumer has suffered loss or damage. This may mean the proposal is out of line with the existing UCT regime, under which the upfront price 'does not include any other consideration that is contingent on the occurrence or non-occurrence of a particular event'.²²

Transparency test for excess

If Treasury does not accept the view that the quantum of the excess under an insurance contract should be reviewable under the UCT regime, the upfront price exclusion should only apply where the quantum of excess is transparently and prominently disclosed in the contract.

This would be similar to the New Zealand laws, under which the price is reviewable for fairness if it is not transparent.²³ This approach could address terms such as the example above, where the excesses cannot realistically be described as the 'upfront price' from the [redacted] per [redacted] would also require a person who has been charged an additional excess to understand the operation of the 'tailored' UCT laws in relation to transparency. They would then need to initiate a dispute with the insurer in order to have the excess(es) tested for fairness. This is clearly not an efficient way to achieve the objectives of this reform.

12. Should additional tailoring specific to either general or life insurance contracts also be considered?

Additional tailoring is not appropriate. We note that excesses are typically not charged under life insurance policies.

Standard form contracts

13. Is it necessary to clarify that insurance contracts that allow a consumer or small business to select from different policy options should still be considered standard form?

14. If yes, do you support this proposal or should an alternative definition be considered?

We strongly support the UCT regime applying to insurance contracts under which the insured can select different policy options. This is common in insurance markets and in other consumer markets where the UCT regime applies. Again, this element of the regime could be detailed in the EM and guidance.

²² ASIC Act section 12BI(3).

²³ As described at page 10 of the proposal paper.



Inclusion of authorities to access medical information

In relation to the meaning of standard form contract more broadly, we support the Parliamentary Joint Committee recommendation that, for the purposes of the UCT regime, the 'insurance contract' should include an authority to access medical information. This is important, as consumers can be particularly vulnerable during life insurance claims and insurers should not continue to gain unreasonably broad access to sensitive medical information.²⁴

Meaning of unfair

15. Do you consider that it is necessary to tailor the definition of unfairness in relation to insurance contracts?

16. Do you support the above proposal or should an alternative proposal be considered? For example, should the approach taken in New Zealand's Fair Trading Act be considered?

We strongly support the specified meaning of unfair under the proposal. Again, this definition could be contained in the EM and guidance.

We support this formulation *only* if the insurer bears the onus of proving that a contract term:

- is reasonably necessary in order to protect the legitimate interests of the insurer, AND
- would not disproportionately or unreasonably disadvantage the insured.

This reflects the onus of proof under the existing regime.²⁵

The important principles and outcomes for this element of the UCT regime are:

- Consistency with the existing UCT regime—to ensure jurisprudence is coherent and the gains made for consumers elsewhere apply to insurers,
- The onus of proof is on the insurer at all points of any test,
- Insurers are incentivised to ensure that contract terms accurately and transparently reflect the risk, as has been the case for other industries,
- Common industry practice does not in itself demonstrate a legitimate business interest,
- Terms that disproportionately or unreasonably disadvantage the insured are deemed unfair, and
- The definition promotes accessibility of the UCT regime for consumers and enables fair outcomes.

The proposed second limb of the fairness test is important to ensure that the UCT regime applies effectively to insurance contracts. It will provide a proportionate response where an insurer argues that a term is reasonably necessary to protect its legitimate interests, but those interests result in disproportionate harm to the consumer, who is the weaker party to the contract.

²⁴ Parliamentary Joint Committee, Recommendation 8.6, p 135.

²⁵ ASIC Act section 12BG(4).



What are legitimate interests?

The extent of a financial institution's legitimate interests was examined in *Paciocco v Australia and New Zealand Banking Group Limited* [2016] HCA 28. The High Court took a broad view of the bank's legitimate interests when deciding whether its honour, dishonour and late fees were unconscionable, unjust or unfair. The Court considered the fees related not only to the banks' operational costs but also its provisioning costs and regulatory capital costs.²⁶ The Court favoured the bank's evidence of the complexity and extent of its costs over the evidence presented on behalf of the customers. If a UCT claim arose in relation to an insurance contract, it is possible that, similarly to *Paciocco*, complex evidence of the nature of an insurance business would be difficult for a consumer to counter. This would be symptomatic of the power imbalance and information asymmetry between insurers and their customers, and would create an unintended barrier for consumers in disputes. If the UCT regime is to effectively protect insurance consumers, it must recognise the challenges they face in obtaining, understanding and interrogating evidence of the insurers' commercial interests and costs.

Another case in which business interests justified a contract term is *Jetstar v Free* [2008] VSC 539. The Supreme Court of Victoria considered the predecessor to the current UCT regime and took into account broader industry practice. The Court decided the term was necessary to protect the business's legitimate interests. The Court stated that the regime was:

[C]entrally concerned with the fairness of the terms of contracts in themselves, in the light of broad business practices in the relevant industry, and in the light of the circumstances in which each relevant contract was made, and not so much with the multifarious personal interests of individual parties to which their contracts might directly or indirectly relate.²⁷

By the rationale of *Jetstar*, the broader impact of contract terms, rather than the individual impact, may be the primary consideration. Where a customer is vulnerable or marginalised, as are many people who Consumer Action works with, the 'legitimate interests' test alone could see broader business interests and practices given greater weight than the extent to which they impact on the consumer in question.

While an unfair contract term declaration can have systemic impact, the broader outcome should not justify unfair terms where more vulnerable people are affected more severely.

In our view, the legitimate interested test could face the risk that an insurer successfully argues that its terms were reasonably necessary to protect its 'legitimate interests' on the basis of very broad considerations. The second limb is therefore a necessary counterbalance.

²⁶ [2016] HCA 28 at para 201 per Gaegler J.

²⁷ *Jetstar Airways Pty Ltd v Free* [2008] VSC 539 at para 119.



Case studies and examples

Car insurance—Exclusion for theft by a person under 30 years of age

General exclusions

The following general exclusions apply to all sections of this policy.

Under this policy there is no cover provided for any loss, damage or liability caused directly or indirectly by or in any way connected with:

...

5. **your vehicle** being driven by a person under 30 years of age if you have selected the 'Driver age restriction' Cover Option (see page 49), unless the driver of your vehicle was:

- driving the vehicle in the course of a mechanical service;
- providing a valet parking service;
- paid by you to repair or test your vehicle where they are qualified to do so;
- an attendant in a car park or car wash service; or
- subsequently convicted of theft or illegal use of your vehicle. [Emphasis added]

CommInsure, *CAR INSURANCE: Product Disclosure Statement (PDS)*, 18.02.2017, pp 55-56.

The last point under this general exclusion allows the insurer to decline a claim when someone's car is stolen or used illegally by someone under 30 years of age, and they are not convicted. It demonstrates why the proposed meaning of unfair for the UCT regime for insurance is appropriate and necessary.

In our view, if the proposed unfairness test applied to this clause:

- Insurer's legitimate interests: The insurer may show the underwriting basis for the clause, for example, the higher risk of damage and loss caused by drivers under 30 years of age.
- Not disproportionately or unreasonably disadvantage the insured: The insurer would need to show why the underwriting justification prevails despite the significant disadvantage that the term causes the insured person, including that:
 - the claim can be denied in full under this clause,
 - theft and illegal use of cars are offences predominantly committed by younger people. making the theft cover under the policy of very narrow,
 - an insured person has no control over whether the car is stolen or used illegally. They certainly have no control over the age of the person who steals the car (as opposed to circumstances where they allow someone to use their car), and
 - an insured person also has no control over whether the theft or illegal use leads to a conviction—this is a matter for police, prosecutors and the Courts. It may be affected by circumstances such as a plea bargain or a Court not recording a conviction for the offender.

In our view, this example from a major insurer's mainstream insurance policy clearly demonstrates the need for insurers to apply a strong fairness test to their products. However, it may also conflict with section 54 of the IC Act, as it allows CommInsure to decline a claim where the conduct of the insured has not caused or contributed to the loss.



Home building insurance—cash settlement

Cash settlement clauses in home building insurance policies allow an insurer to elect to pay the claimant in cash or vouchers, rather than the insurer repairing or rebuilding the home. These clauses are drafted in various ways by various insurers, which can make a significant difference to people's claims experiences and outcomes.

Monetary settlements and the meaning of cost to us

If we decide to pay you what it would cost us to rebuild or repair (or if we give you a voucher, store credit or stored value card for what it would cost us), we will pay you (or give you a voucher, store credit or stored value card for) the amount that we determine to be the reasonable cost of repairing or rebuilding. The amount we determine to be the reasonable cost will be the lesser amount of any quotes obtained by us and/or by you for the rebuild or repair.

Discounts may be available to us if we were to rebuild or repair.

...

Reasonable cost

means the amount we determine. Reasonable cost is the lesser amount of any quotes obtained by us and/or by you.

Discounts may be available to us through our suppliers.

AAMI, Home Building Insurance, Supplementary Product Disclosure Statement, 19 January 2018

This may be considered an unfair contract term, because:

- there is a power imbalance and information asymmetry between the insurer and the insured—it is very difficult for the insured to know whether the settlement offered by the insurer is adequate to repair or rebuild their own home,
- the insurer can unilaterally elect to cash settle the claim, rather than repairing or rebuilding the home, despite the claimant's wishes, and
- the insurer can give the claimant cash or store credits, cards or vouchers, meaning the claimant may have no choice of supplier.

According to the test in the proposal paper, the insurer would have to show that the underwriting basis of the clause is justified when balanced against the potential detriment a consumer could suffer under this clause.

The unfair impact of a term like this can be amplified by the vulnerable circumstances people are in when they make home insurance claims. A person may be homeless when making a home insurance claim, for example, after experiencing a natural disaster. People have reported to Consumer Action that they feel pressured to make a quick decision about accepting a settlement. They can also struggle to find appropriate suppliers or tradespersons, particularly in regional, rural and remote areas or after a disaster which has affected many homes. Insurers can cash settle because it is too difficult to find a supplier or tradesperson, even though a claimant will have exactly the same problem. More broadly, a claimant may be shocked to find that the settlement amount offered for their badly-damaged home is inadequate to repair the building, despite the fact that they have an adequate sum insured under their policy.

Unfair contract terms such as these can significantly damage public trust and confidence in insurers. They can mean insurers are not there for their customers when they really need them. People's claims experiences and



the benefits paid show the true value of an insurance product—and this value can be eroded by unfair contract terms.

Travel insurance—Blanket mental health exclusions

Ingram v QBE Insurance (Australia) Ltd (Human Rights) [2015] VCAT 1936

Ella Ingram booked an overseas school trip, then had to cancel it several months later when she was diagnosed with depression.

Ella claimed the costs of cancelling her trip from QBE, her travel insurer. QBE declined her claim on the basis of a blanket exclusion of mental illness.

The Victorian Civil and Administrative Tribunal (**VCAT**) found QBE had discriminated against Ella under the Equal Opportunity Act 2010 (Vic), which includes equivalent 'unjustifiable hardship' and lawful discrimination provisions to federal discrimination laws. QBE did not show it would suffer unjustifiable hardship without the exclusion, and did not have the data to justify it.

Ella was entitled to over \$4,000 for economic loss and \$15,000 for hurt and humiliation, and the fear QBE's decision caused her about future discrimination. However, VCAT did not make an unlawful discrimination declaration, meaning the decision did not have broader implications.

FOS determination 428120, 31 March 2017

An Australian man went on a trip to Canada. While he was there, he experienced an acute psychotic episode. It was the first time this had happened to him. He went to hospital and was diagnosed with bipolar disorder. He had to return to Australia with his parents, and claimed on his travel insurance for the costs of his medical treatment, cancelling the trip and returning to Australia.

The insurer denied his claim under its blanket exclusion of claims arising from or related to 'depression, anxiety, stress, mental or nervous conditions'. The man disputed this and took his complaint to FOS.

FOS found that the blanket mental illness exclusion was discriminatory. The insurer would not suffer unjustifiable hardship without the exclusion. Similarly to Ella Ingram's case, the insurer could not show any data or other relevant factors to justify the blanket exclusion.

The man was entitled to more than \$8,800 in cancellation fees and medical and other expenses. He was also awarded \$1,500 for non-financial loss because the insurer's denial of the claim was 'unreasonable and caused an unusual degree of inconvenience and pressure'.

Blanket mental health exclusions such as these are another clear example of what we would consider to be unfair contract terms. Applying the test in the proposal paper to these examples:

- **Insurers' legitimate interests:** Insurers may be able to show the underwriting basis of these clauses, for example by showing actuarial or statistical data which meets the requirements of section 46 of the *Disability Discrimination Act 1992*. However, insurers have not shown that they have the data to satisfy this requirement for blanket mental health exclusions. Some insurers do not have blanket mental



health exclusions in their policies, meaning insurers have taken different approaches to underwriting the same risk.

- Not disproportionately or unreasonably disadvantage the insured: It may be difficult for an insurer to show that the clause is proportionate, particularly where an insured person has no pre-existing mental illness.

Insurers have not demonstrated that they are complying with the existing discrimination laws. Those laws also do not expressly weigh up the insurers' interests against their customers' interests. While the decisions above have prompted some voluntary changes to travel insurance policies, clearly a more tailored, preventative regulatory approach is needed to address these types of clauses. The UCT regime would provide this.

New Zealand approach

We do not support the NZ approach. Consumer NZ, in its recent submission to the review of the Insurance Contracts Law, pointed to ongoing unfair terms in insurance contracts. These include terms which give insurers the unilateral right to end a contract, terms which prevent consumers from cancelling a policy and receiving a refund, and multiple excesses which can take the total excess beyond the value of the claim.²⁸ We would not want to see a UCT regime which delivers these types of outcomes.

17. Should tailoring specific to either general or life insurance contracts be considered?

The proposed test is broad enough to apply effectively to both life and general insurance.

Terms that may be considered unfair

18. Do you consider that it is necessary to add specific examples of potentially unfair terms in insurance contracts?

19. Do you support the kinds of terms described in the proposal or should other examples be considered?

The list of terms which may be unfair is important, to make the practical operation of UCT regime clear.

We note that the current list of terms in section 12BH(1) of the ASIC Act apply to consumer contracts broadly. Terms specific to insurance contracts could be included in section 12BH(1) or alternatively be prescribed under the ASIC Regulations in accordance with section 12BH(2).

The examples provided in the proposal are sound and capture some of the most common unfair terms that we see in insurance contracts.

²⁸ Consumer NZ., *Review of Insurance Contract Law Issues Paper*, 13 July 2018.



Other terms which should be reflected in the list include:

- Terms which require the consumer to pay an excess or other amount to the insurer before the insurer will pay a benefit. This can prevent people in financial hardship from having their claims paid.
- Terms which require a claimant to pay the costs of investigating a claim, if the claim is withdrawn or declined. This could act as a disincentive to making a claim. In addition, claims investigation is a cost which insurers should bear in their own businesses.
- Terms which restrict the consumer's right to cancel the policy, including terms which enable the contract to be automatically renewed where the deadline to cancel the policy is unreasonably short.
- Terms (for example, in car insurance policies) which require an insured to take 'all reasonable precautions to avoid the incident'. This is a higher threshold for the insured person than the current legal requirement. The term may be misleading and deceptive and could deter people from making claims.
- Medical definitions which are out-of-date and cannot be met.
- Terms in total and permanent disability (TPD) insurance policies which 'offset' the benefit paid against the benefit paid under any other TPD insurance policies. These clauses mean that a person may be paying premiums while the insurer never intends to pay them a benefit.

20. Should tailoring specific to either general or life insurance contracts also be considered?

Some of the examples above are more relevant to certain insurance policies and should be drafted to prevent the unfair outcome that a consumer would experience if the term were applied.

Remedies for unfair terms

21. Do you support the remedy for an unfair term being that the term will be void? Is a different remedy more appropriate (for example, that the term cannot be relied on)?

22. Do you consider it is appropriate for a court to be able to make other orders?

23. Should tailoring specific to either general or life insurance contracts also be considered?

We support the approach in the proposal paper. It strikes an appropriate balance of consistency with the existing regime and ensuring fair consumer outcomes.

It is important for the UCT regime to provide fair outcomes, which may not include voiding an unfair contract term in an insurance policy. For example, voidance could mean that the policy benefit is not paid in full.

We note that under the existing UCT regime a Court can make a range of orders it thinks appropriate if a party tries to rely on a term which has been declared unfair. These include injunctions, compensation and redress to non-party consumers.

We also note that section 15 of the IC Act may operate to prevent ASIC from taking action against an insurer for unconscionable conduct and/or misleading and deceptive conduct if the insurer attempts to rely on an unfair term. The amending legislation should ensure that all other ASIC Act protections apply in relation to the review of insurance contracts.



Third-party beneficiaries

24. Do you consider that UCT protections should apply to third-party beneficiaries?

25. Do you support the above proposal or should an alternative proposal be considered?

We support the proposal that the UCT regime cover third-party beneficiaries of insurance contracts.

26. Superannuation fund trustees may have substantial negotiating power and owe statutory and common law obligations to act in the best interest of fund members. Do these market and regulatory factors already provide protections comparable to UCT protections such that it would not be necessary to apply the UCT regime to such products?

The UCT regime must cover life insurance products in superannuation.

Over 12 million people are covered by life insurance in superannuation.²⁹ It is clear that the duty of fund trustees to act in their members' best interests is not operating effectively. This sizable group of people require more protections from the unfair operation of insurance policy terms.

The Productivity Commission recently reported [redacted] erid [redacted] ce in superannuation. These included:

- unnecessary, duplicate, inappropriately bundled and 'zombie' policies,
- 'extremely complex and incomparable policies',
- problems for members dealing with funds in relation to insurance,
- poor application of risk premiums, and
- little or no tailoring of policies to member cohorts.

The Productivity Commission stated:

These outcomes are hard to reconcile with the legal obligations on super fund trustees to act in their members' best interests and to ensure that insurance does not inappropriately erode their members' balances.³⁰

The best interests duty is clearly not a strong enough protection and is not adequately enforced by regulators, particularly in the context of conflicts of interests caused by certain ownership structures and business models. There is no effective 'preventative' consumer protection measure, and no significant 'cure' for consumers who have suffered harm.

There is more broadly a gap in protections to prevent people from experiencing claim shock due to a policy term being unfairly applied. Individual consumers can take insurance claim disputes to the Superannuation Complaints Tribunal/AFCA. However, there is no ASIC oversight of claims handling. People with their life insurance in superannuation are not covered by the Life Insurance in Code of Practice, and there is currently

²⁹ Productivity Commission. *Superannuation: Assessing Efficiency and Competitiveness—Draft Report Overview*, April 2018, p 20.

³⁰ Productivity Commission, 2018, pp 21-22.



no complaints-handling authority for the Insurance in Superannuation Voluntary Code of Practice. Not all funds are signatories to the voluntary Code. The current protections for people who have their life insurance in their superannuation are woeful.

This is the stark reality for the many people who rely on life, TPD and/or income protection insurance to support them and/or their families if they are struck by tragedy. The stakes are too high and the failures of existing protections too obvious to leave this to the market and existing laws. Both have failed people. The case is clear for UCT protections to cover life insurance in superannuation.

Tailoring for specific insurance contracts

27. Do you consider that any other tailoring of the UCT laws is necessary to take into account specific features of general and/or life insurance contracts?

The EM and guidance will be important in ensuring the effective operation of these reforms, but insurance contracts do not need a tailored regime. The existing regime applies to a vast and varied range of industries. Insurers are not unique and their businesses do not justify a separate regime.

28. Do you agree that unilateral premium adjustments by insurers are unfair in circumstances in which the premium increase is within the limits and under the circumstances specified in the policy?

It is unclear whether we can support this proposal without further detail. Under this proposal, whether or not a premium increase is 'fair' appears to be contingent on other terms and circumstances in the policy. This is in line with the operation of the existing regime. However, the details of this exemption will be critical to the effect of it on consumers.

We note that the current requirement that life insurers unilaterally alter premiums on a 'simultaneous and consistent basis' only, not on an individual basis, must continue in addition to the UCT regime.³¹

If unilateral premium adjustments are not to be considered unfair where the premium increase is within the limits and circumstances of in the policy:

- the life insurer should demonstrate the assessment of risk, including health, actuarial or statistical data, and
- terms relating to premium increases should be clear and transparent. Insurers should specifically highlight them when a consumer enters into a contract and when any increases are applied.

³¹ *Life Insurance Act 1995* (Cth), sections 9A(3) and (5).



Transitional Arrangements

29. Is a 12-month transition period adequate? If not, what transition period would be appropriate?

30. Are the transition arrangements outlined above appropriate or should alternative transition arrangements be considered?

A 12-month transition period is adequate, considering the urgent need to address the imbalance and consumer detriment caused by unfair insurance contract terms. The Parliamentary Joint Committee recommended that 'ASIC engage with life insurers to begin removing unfair terms from life insurance contracts as soon as possible'.³² General insurers should similarly have started the process of reviewing and improving their contracts.

ASIC oversight

ASIC oversight of changes to insurance contracts and consumer costs during the transition period will be critical.

ASIC oversight will provide significant benefits to insurers and consumers during the transition of insurance contracts to the UCT regime. In particular, ASIC's ~~review of contracts and costs~~, detailed guidance on compliance, and examination of the underwriting or other basis of changes to contract terms will help to ensure that insurers comply with the UCT regime from its commencement.

31. What will insurers need to do during the transition period to be ready to comply with the new UCT laws?

Insurers should be proactively working with ASIC to identify unfair contract terms and improve their contracts. This would follow the lead of the many other industries which adapted when the UCT regime was introduced.

32. Should tailoring specific to either general and/or life insurance contracts be considered?

The proposed transitional arrangements appear to be appropriate for general insurance contracts which are renewed annually.

However, depending on the legislative drafting, the UCT regime could be ineffective for life insurance contracts if the transitional arrangements operate to significantly delay or avoid the regime applying to guaranteed-renewable life insurance policies

The following issues may arise with guaranteed-renewable life insurance policies under the transitional arrangements:

- **Renewed contracts:** It is unclear whether ongoing guaranteed-renewable life insurance policies will ever be brought within the UCT regime under this element of the transitional arrangements.

³² Joint Parliamentary Committee , Recommendation 3.2.



- Contract variations: Applying the regime to varied terms could mean that the updated terms in a contract are reviewable, while terms which remain unchanged are not. If some contract terms are reviewable for fairness and other terms are not, the regime as it applies to life insurance could operate contrary to the requirement of the existing UCT regime that a term is assessed in the context of the contract as a whole.

There is a risk that many people remain on guaranteed-renewable life insurance policies for years or decades, and the UCT regime may never apply substantively to their contracts. Alternatively, the UCT regime may apply to some but not all terms in the contract, which will create uncertainty and inconsistency with the existing regime.

Legacy products should not be carved out through any unintended application of the transitional arrangements.

The transitional arrangements should ensure that the regime applies to life insurance contracts promptly and comprehensively. People should not be disadvantaged because they took out policies a long time ago and, for example, those policies contain outdated medical definitions.

Please contact Susan Quinn at Consumer Action on [REDACTED] or [REDACTED] if you have any questions about this submission.

Yours sincerely,

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