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Unfair Terms in Insurance Contracts: Options Paper
Corporations and Financial Services Division
The Treasury
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PARKES
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Introduction

National Legal Aid (NLA) represents the Directors of the eight State and Territory legal aid commissions (commissions) in Australia. The commissions are independent statutory authorities established under respective State or Territory enabling legislation. They are funded by State or Territory and Commonwealth governments to provide legal assistance to disadvantaged people.

NLA aims to ensure that the protection or assertion of the legal rights and interests of people are not prejudiced by reason of their inability to:

- Obtain access to independent legal advice;
- Afford the appropriate cost of legal representation;
- Obtain access to the Federal and State and Territory legal systems; or
- Obtain adequate information about access to the law and the legal system.

Executive Summary

NLA welcomes the opportunity to respond to Treasury's Options Paper on the application of unfair terms legislation to consumer contracts in insurance.

NLA applauds the recent enactment of landmark legislation, the *Australian Consumer Law*, in Australia to regulate unfair terms legislation. The new legislation will protect all consumers in Australia from unfair terms in the standard form consumer contracts but it does not currently apply to consumers of insurance products.

NLA supports the urgent rectification of this anomaly by amending the *Insurance Contracts Act*[1], to ensure that the *Australian Consumer Law* unfair terms legislation applies equally to insurance contracts, as set out in **Option A**.
Option A is the only option that can provide an effective and proportionate response to the endemic problems existent in the current insurance market.

The basis of our submission is that there is nothing special or unique about insurance as a financial product or as a financial market that would warrant moving unfair terms legislation outside the current legislative regime.

Proposals outlined that lead to solutions based on either self-regulation (Option D), manipulation of existing legal concepts like good faith (Option C) or a special form of unfair terms regulation for insurance (Option B)[2] are, in our view, based on a number of false assumptions about insurance, the markets they operate in and the current legislative regime that governs those markets.

In addition, a consistent approach to regulation of unfair terms in contracts would provide considerable benefits to consumers—particularly disadvantaged consumers—because it would simplify the principles and regulatory arrangements that consumers are required to understand in order to enjoy their basic rights.

For these reasons, we support Option A as the only viable option, and the only option that has been subject to rigorous assessment by the Productivity Commission.

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[1] By repeal of s 15 *Insurance Contracts Act* to clarify the operation of *Australian Consumer Law* provisions.
[2] Though Insurance Council does note that it sees Option B as less attractive than Option C or D. See ICA submission to 'Unfair Terms in Insurance Contracts – Options Paper' at p.3

Background

- Expertise in consumer laws – unfair terms legislation

Legal Aid Commissions have been long-standing advocates for the need to introduce provisions about unfair terms in contract legislation. Legal Aid Commissions responded to the Standing Committee of Officials of Consumer Affairs Working Party on Unfair Contract Terms in early 2004; the Productivity Commission's Draft Report of the Inquiry into Australia's Consumer Protection Framework in 2008; and to an issues paper on Australian Consumer Law - Fair Markets – Confident Consumer from the Standing Committee of Officials of Consumer Affairs in 2009.

- Expertise in insurance consumer law

Legal Aid Commissions have specific policy expertise and casework experience to respond directly to the insurance issues raised in the Options Paper, including:

- Responding to the 2004 Insurance Contracts Act Review[3]
- Responding to the 2004 General Insurance Code of Practice Review[4]
- Responding to the Independent Review of Insurance Ombudsman Service in 2005[5]
- Responding to Productivity Commission's Inquiry into the Australia's Consumer Policy Framework in 2006[6]
- Responding to the Draft Report of the Productivity Commission into Australia's Consumer Policy Framework in 2008[7]

[3] Submission(s) into 'Review of *Insurance Contracts Act'*, Review of s 54 and Review of sections other than s 54, Legal Aid NSW, 2004; Submission to the Review of the Insurance Contracts Act – Response to Issues Paper, CFA, April 2004; Submission to the Review of the Insurance Contracts Act –Response to Proposals Paper, CFA, June 2004

[4] CFA members were part of a Working Committee into Review of the Code

[5] Submission responding to Issues Paper on the Review of the IOS, Legal Aid NSW, May 2005

[6] Submission to Productivity Commission Inquiry on Consumer Policy, Legal Aid Commission of NSW, June 2007

[7] Submission to Productivity Commission on Draft Report on Consumer Policy, Legal Aid Commission of NSW February 2008

- Responding to the Insurance Council of Australia's application to the ACCC for authorisation of a common definition of 'inland flood' in 2008[8]

- Responding to the consultation paper prepared by Commonwealth Treasury An Australian Consumer Law: Fair Markets – Confident Consumers in 2009[9]

- Responding to consultation on the draft Trade Practices Amendment (Australian Consumer Law) Bill (2009)[10]

- Responding to the Independent Process Review of Insurance Ombudsman Service in 2008[11]

- Responding to call for submissions by Senate Economics Legislation Committee hearing on Australian Consumer Law Bill 2009 including responding to requests to attend that hearing[12]

- Responding to the 2009 General Insurance Code of Practice Review[13]

- Responding to the Insurance Contracts Act Bill (2009)[14]

Commissions also have considerable casework experience in broader consumer law.

[8] Joint Consumer Submission to ACCC re ICA application for common definition of Inland Flood, August 2008
[9] Submission to Treasury re Australian Consumer Law, Legal Aid NSW, June 2009
[10] Submission to Treasury on draft Australian Consumer Law Bill (2009), Legal Aid NSW, May 2009

[12] Submission to Senate Economics Legislation Committee, *Trade Practices Amendment (Australian Consumer Law) Bill 2009*, NLA, August 2009
[13] Joint Consumer Submission to the Review of General Insurance Code of Practice, ILS, July 2009
[14] Joint consumer Submission to the Review of the *Insurance Contracts Bill* (2009)

Outline

This paper is divided into three parts:

Part 1 - Scope of the problem - widespread unfair terms in insurance (Response to Q 1 & 4) & current regulation (Response to Q 2)

Part 2 - Response to Option A - implementation of generic national unfair terms regulation to insurance (Response to Q 5) & general response to Options B & C

Part 3 - Further response to Options B, C & D - 'regulatory breakout' proposals (Response to Q 6, 7 & 8)

Part 1 - Scope of the problem - widespread systemic unfair terms in insurance & current regulation

Response to Consultation Question 1 & 4 - Evidence of widespread systemic unfairness in insurance policies & the cost-benefit of the status quo remaining

There is overwhelming evidence on the public record, which documents in clear and unambiguous terms the detriment that consumers have suffered due to harsh or unfair terms in insurance policies. This evidence includes:

1. Consumer submissions to the Senate Economics Committee into Australian Consumer Law on the application of unfair terms legislation to insurance[15]
2. Consumer submissions into the 2009 General Insurance Code of Practice[16].
3. Consumer submissions into the 2004 Review of Insurance Contracts Act[17]

[15] Submission to Senate Economics Legislation Committee, *Trade Practices Amendment (Australian Consumer Law) Bill 2009*, NLA, August 2009; Submission to Senate Economics Legislation Committee, *Trade Practices Amendment (Australian Consumer Law) Bill 2009*, CALC, July 2009, Submission to Senate Economics Legislation Committee, *Trade Practices Amendment (Australian Consumer Law) Bill 2009*, Insurance Law Service, August 2009

[16] Insurance Law Service submission to General Insurance Code of Practice, 2009

[17] Response to Review of Insurance Contracts Act on sections other than s 54, Legal Aid Commission of NSW (2004)

4. Annual Reviews of the Insurance Ombudsman Service (formerly Insurance Enquires & Complaints Ltd and now Financial Ombudsman Service)[18],
5. Determinations of the Insurance Ombudsman Service (formerly Insurance Enquires & Complaints Ltd and now Financial Ombudsman Service)[19],
6. Trade Practices Commission Life Insurance and Superannuation report[20]
7. Information Brochures produced by Insurance Ombudsman Service[21] and Insurance Law Service[22] and Legal Aid Commission of NSW[23]

NLA suggests that in the assessment of the extent of the problem for Australian consumers, particular attention should be given to the report card on the state of insurance industry policies that has been provided each year by Insurance Ombudsman Service[24], as set out in its Annual Reports. We set out selected commentary from the Insurance Ombudsman Service which outlines key concerns that decision makers have had about consumer detriment arising from harsh or unfair terms in insurance contracts **(see Annexure 1).**

It is also noteworthy that whilst the Options Paper quite rightly points out that there are payment rates of up to 98%, this does not highlight or address the quantitative or qualitative loss associated with refused claims. This is a significant omission given the size of the insurance markets. For example, in 2007-2008[25], there were 31,259,018[26] general insurance policies issued and 3,172,539[27] claims made, which resulted in refused claims totalling 69,433[28]. Out of the 69,433 refused claims only 2,038 consumers lodged a dispute with FOS[29]. Even when one takes into account overturn rates at IDR, it leaves a significant number of disaffected consumers without redress.

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[18] See IOS (IEC) Annual Reports from 1992 – 2008. For instance, Panel Chair's Report, 2004 Annual Report IOS
[19] See IOS (IEC) Annual Reports from 1992 – 2008. For instance, Panel Chair's Report, 2004 Annual Report IOS
[20] Trade Practices Commission Life Insurance and Superannuation Report, December 1992
[21] For instance, see "A Guide to Travel Insurance", IOS (2006)
[22] See for instance Insurance Law Facts Sheets – 'What Can I Do if my Home/Contents Claim is Refused?'
[23] See 'Turning the Tide: Storms, Flood - Insurance & You' , Legal Aid NSW
[24] Now Finnancial Ombudsman Service and formerly known as Insurance Enquiries Complaints Ltd
[25] IOS Annual Report, 2007-2008
[26] Op cit , p.17
[27] FOS General Insurance Code of Practice, Overview of 2007-2008 Financial Year, p. 6
[28] Calculated by deducting 3,103,106 (claims paid) from 3,172,539 (claims made): FOS General Insurance Code of Practice, Overview of 2007-2008 Financial Year, p. 6
[29] Insurance Ombudsman Annual Review 2007-2008, p.1

What is more difficult to gauge is what percentage of refused claims would be caught by the unfair terms legislation. Given the sophisticated nature of the test in the ACL, which is a proportionate and subtle approach that does not penalise terms that are necessary to protect the legitimate business interest or relate to key subject matter, we would expect it to have a modest impact on the number of refused claims for which a remedy may exist.

We would expect the unfair terms legislation to have a particular impact on policies in travel insurance and credit card insurance, where there is well documented concern by the Insurance Ombudsman Service about 'rubbery terms', over a number of years[30].

A further level to the analysis of the detrimental impact that harsh or unfair terms in insurance policies has on the Australian community is in relation to the particular markets in which particular insurance products operate. To demonstrate, we identify ongoing consumer concerns in the key markets of motor vehicle and home insurance:

- Motor vehicle policies - consumer concerns

Australia has one of the highest rates of car ownership in the world, with more than one in two Australians owning a car.[31] Not surprisingly therefore motor vehicle policies constitute a substantial proportion (around 39-40%) of policies issued[32] and disputes about claims made under these policies constitute around 33-39% of disputes.[33] It is well recognised that Australia's long distances and relatively low density cities contribute to our dependence on cars and that a significant proportion of personal income is invested in buying and running a car. Consequently the loss, of or damage to, a car has a significant impact on Australian consumers.

[30] See Annexure 1 to this Submission
[31] Australian Bureau of Statistics "Australia at a Glance – 2008" available at http://www.abs.gov.au/websitedbs/D3310114.nsf/home/year+book+products?opendocument#from-banner=LN Proportion calculated as number of registered passenger vehicles per head of population in 2006.
[32] This information was reported in the Code of Practice statistics in the years 2004-2006. These statistics are published in the Annual Reviews of the EDR.
[33] This information has been consistently recorded by the EDR body.

Recent data collected by the Local Court of NSW indicates motor vehicle accidents relating to uninsured drivers as one of the top three types of disputes before the Local Court[34]. Many of these drivers present at Legal Aid advice clinics. Our experience suggests that a significant portion of drivers who present as 'uninsured' in the Local Court have taken out comprehensive insurance, but have been informed following an accident that the policy does not cover the specific incident or circumstances. In at least some cases this is due to terms of insurance contracts that would reasonably be considered to be unfair.

- Home building - consumer concerns

There is significant emotional and financial investment in the purchase and ownership of one's own home. The loss of, or damage to, a home can have a devastating impact due to the circumstances giving rise to the loss (which may include flood, storms and bushfires), as well as the need to find new shelter and rebuild one's life. Replacement or repair to the home can cost tens to hundreds of thousands of dollars. Adequate insurance is critical to reducing the impact of damage to the home. Home building policies represent about 20% of policies issued and disputes about these policies represent about 20% of disputes.[35]

Our experience is that there is significant financial hardship associated with refused claims on home and contents policies. The reality being that if the insurer refuses such a claim, particularly a home claim, there is little likelihood that consumers, particularly disadvantaged consumers, will have the financial means to keep and rebuild the home. The stress, uncertainty and concern relating to difficulties arising with ambiguous wording in policies often leads to extended (and unnecessary) delays in paying such claims. This was borne out most recently in Victoria, where Victoria Legal Aid in conjunction with community sector workers advised clients in respect of the 2009 Victorian bushfire disaster. Whilst most insurers were reasonably good at ultimately paying the claims, 'rubbery clauses' left some consumers wondering what their rights were and whether they would be covered. Evidence given by Mr Denis Nelthorpe at the Victorian Royal commission into Bushfires directly addressed these concerns.[36]

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[34] ADR Blueprint Discussion Paper, NSW Attorney General's Office, April 2009 at p.30
[35] According to Code of Practice statistics reported in Annual Reviews.
[36] See witness statement of Mr Denis Nelthorpe to Victorian Bushfires Royal Commission. particularly at para 31-35. The observations of Mr Nelthorpe were accepted in the Recommendations by Special Counsel assisting the Commission: see Transcript at 16 April 2010

The issue of refusal of claim on the basis of flood exclusion has been a matter of considerable public concern for some time. For example, during the 1998 Wollongong floods in NSW, Legal Aid NSW conducted large scale negotiations to achieve fairer outcomes for consumers whose claims were rejected by insurers on the flood exclusion.[37] The relative success in those matters has not, however, redressed the underlying problem. Legal Aid NSW is frequently required to assist consumers following major floods, and there continue to be significant differences in the approaches of major insurers to claims, even in relation to the same flood.

The "flood" issue can now also seen in the context of "climate change" and increased damage to homes as a result of other environmental factors or extreme weather events – storms and cyclones, bushfires fire, drought's effect on soil (leading to subsidence, erosion). The most recent FOS review refers to an increase in such claims and refers to them as "large insurance claims events".[38] The reality for consumers in Australia is a growing need for policies with fair terms that protect them from disaster events.

Existing regulation that affects unfair terms in insurance contracts (Response to Consultation Question 2 & Question 5)

The existence of provisions within the *Insurance Contracts Act* such as s 13 and s 14 and s 35 and s 37 have been used in earlier debates on this topic as a basis for justifying why unfair terms regulation is considered unnecessary.[39] Those provisions are being relied upon as the possible legislative basis to justify a regulatory breakout, as defined in Options B and C.

In our view, to attempt to rely upon principles such as good faith and standard cover as a basis for developing 'softer', industry-friendly unfair terms provisions (Option B) or a morphed good faith principle (Option C), carries significant risks. Concepts such as good faith and standard cover have not succeeded in protecting consumers from unfair terms in contracts. Option A is the only alternative that is available to achieve the government's objective in this area.

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[37] *'Remembering the Corrimal Floods - 10 years* on' 10 page Special Report, Illawarra Mercury,
[38] FOS 2008-2009 Annual Review at 27
[39] See for instance ICA oral and written submissions to Senate Economics Legislation Committee, *Trade Practices Amendment (Australian Consumer Law) Bill 2009*, (Hansard) 26 August 2009

- Duty of utmost good faith ss13, 14 Insurance Contracts Act

In order to understand the inherent risk in relying on good faith as a viable basis for relief from unfair terms (Option C), it is instructive to consider the development of the *Insurance Contracts Act* which highlights the inherent flaws of the current legislative provisions in protecting consumers from unfair terms.

At the time of the Australian Law Reform Commission report into insurance in Australia in 1980, it was hoped that the duty of utmost good faith[40], including the development of a specific prohibition within the *Insurance Contracts Act* on an insurer relying on any term in breach of the duty of utmost good faith[41], would provide sufficient inducement for insurers to draft on fair terms[42]:

Within a decade of enacting the new legislation, however, Parliament was already voicing the concerns of consumer advocates about the wisdom of enacting provisions which required the consumer (the weaker party to the transaction), to take *pro-active* steps to have an insurer held to account in relying on a term which would breach the duty of utmost good faith.

> "**The Act has been criticised by consumers, largely because it is costly and cumbersome for individuals to take legal action where a breach of the act has occurred.**[43] **[Emphasis added]**

[40] s13 *Insurance Contracts Act* (Cth) 1984
[41] s 14 *Insurance Contracts Act* (Cth) 1984
[42] ALRC 50 at para 51
[43] *Hansard*, Parliament of Australia (Cth) Insurance Laws Amendment Bill (No 2) 1994

Those comments in 1994 are concerns that still hold true for the concept of utmost good faith today. Over the last three decades, very few consumers have taken the significant step of suing their insurer to enforce their legal rights under s 14.[44] This is not surprising given very few consumers have the means or the motivation to risk the consequences of an adverse costs order in Court proceedings. It is not surprising, for example, that the current leading High Court case on utmost good faith was a dispute between one major insurer against another.[45]

Equally, in low cost jurisdictions such as the Financial Ombudsman Service, most consumers do not argue good faith as a basis for relief.[46] In our experience, most consumers do not understand their rights under that provision to make such a claim. In a number of cases the concept of good faith is also not the appropriate legislative tool to extract relief for harsh or unfair terms. Further, our analysis of the history of decision making at the Financial Ombudsman Service is that it has not commonly relied upon using good faith as a basis for consumer relief from harsh or unfair terms.[47]

Under the *ASIC Act,* ASIC (and its predecessor Insurance & Superannuation Commissioner) has had power since 1994[48] to intervene in respect of issues relating to good faith. Despite this, we are unaware of litigated ASIC intervention against an insurer for breach of utmost good faith provisions.

- Standard cover, s35 Insurance Contracts Act

The protection that s35 hoped to provide consumers was a prescribed contract with minimum standards on key clauses – essentially setting a minimum prescribed standard of fairness for specified general insurance contracts.

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[44] For commentary on s 13 and s 14 see Annotated Insurance Contracts Act (4th Ed), Mann 2003; Australian Insurance Law (1st Ed), Pynt.

[45] The leading High Court case at present on good faith is the case of *CGU insurance Ltd v AMP Financial Planning Pty Ltd* [2007] HC 36. However, whilst this decision contains some of the most current pre-sentiment of the Court on the importance of the duty of utmost good faith, the reality is that such comment was dicta. The Court found that despite the undesirable behaviour of CGU, AMP was not able to rely on a breach of utmost good faith as a means of succeeding in the claim

[46] Our analysis of decisions from FOS over the last 18 months was that good faith was used sparingly as a basis for relief.

[47] See Annual Reviews from Financial Ombudsman Service available at fos.org.au

[48] s11B *Insurance Contracts Act* - see Mann P, Annotation Insurance Contracts Act at [11B.10]

The very significant limitation on the usefulness of s 35 to protect consumers is that an insurer, who clearly informs an insured in writing at the time of policy inception of derogation from standard cover, will have complied with that provision.[49]

The interpretation given to the words 'clearly informed in writing' in s 35 has been that an insurer who serves on an insured a copy of an insurance policy (which contains such exclusion clauses) *at the time of inception*[50], is likely to have complied with s 35. [51]

In practical terms, the impact of the *Hams* decision is that contracts are not necessarily drafted according to the reasonable expectation of consumers; they are drafted on terms suitable to insurers, with exclusions contained and served on consumers as part of the written policy subsequent to the purchase of the product. Equally, as insurers are not required to provide notice of derogation at the time of renewal, consumers may never see the document containing the derogation more than once.[52] As very few consumers read their policies[53] and even fewer can understand the interplay of related sections, standard cover has not provided significant relief for consumer from unfair terms.

On both counts, the *Insurance Contracts Act* has failed to provide protection for consumers from terms that are unfair.

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[49] s 35 (2) *Insurance Contracts Act*

[50] s 69 *Insurance Contracts Act provides* that provision of a copy of the policy within 14 days of the date of the contract (usually completed over the phone) is sufficient compliance with this requirement.

[51] *Hams v CGU Insurance Ltd* [2002] NSWSC 273 per Einstein J

[52] S 21 A *Insurance Contracts Act*

[53] There is now a considerable body of work in Australia and UK documenting and accounting for consumer behaviour in this regard: see for instance L Griggs 'The [ir]rational consumer and why we need national legislation governing unfair contracts terms' (2005) 13 CCLJ 51.

The Insurance Ombudsman Service made the same observation on consumers when it stated:

> "The fundamental principle relevant to all insurance disputation on which all parties agree is that no-one ever reads the policy before a claim is made." (2005) IOS Annual review, Addendum, p.4

Part 2 - Implementation of national Unfair terms legislation as the only viable proposal (Option A)

Generic national *Unfair terms* legislation - Option A
(Response to Consultation Q 5)

NLA supports Option A as the only effective legislative response to the issue of unfair terms in insurance contracts, in that Option A is the only proposal that:

1. Implements Productivity Commission Recommendations;
2. Implements COAG & MCCA Recommendations;
3. Implements Senate Economics Committee Recommendations;
4. Implements *good consumer policy*

- Option A - implements Productivity Commission Recommendations

Option A is the only option proposed that has been properly cost-assessed by the Productivity Commission. The economic benefits to the country of national generic unfair terms legislation as part of the broader reforms outlined in Australian Consumer Law package was estimated as a net gain to the Australian community of between $1.5 billion and $4.5 billion per year.[54] The Productivity Commission assessed the benefit to the Australian economy of enacting generic, national unfair terms legislation. It concluded

> " There is little reason for any variation in the content of the generic consumer law.
>
> The generic law reflects broad notions of efficiency, fairness and equity, which the vast majority of consumers and businesses would regard as appropriate and reasonable irrespective of where they live or trade.
>
> The broad, principles-based, nature of the generic law allows for its application to a wide variety of particular circumstances. This largely removes

[54] Productivity Commission "Review of Australia's Consumer Framework" Final Report- (30 April 2008) Australian Government Canberra Vo 2, p.353

any case for variations in the law itself to account for specific local requirements."[55] [Productivity Commission's emphasis]

The Productivity Commission specifically warned against industry carve-outs from the operation of national generic consumer legislation. Options B, C and D are in effect industry carve-outs. As such, Options B, C and D are exposed to the following specific criticism of the Productivity Commission:

"Differences in enforcement intensity and/or priorities at the jurisdictional level can similarly lead to divergent requirements for businesses (and variable outcomes for consumers).

The costs of divergences in the requirements or application of the generic law should not, of course, be overstated. Even the more significant differences may not necessarily require businesses that adhere to ethical standards to employ tailored compliance strategies.

Nonetheless, as indicated above, the cumulative costs of even individually small differences can be material. And because many of them are seemingly needless, they can also be a source of significant frustration for businesses. More importantly, a continuation of the recent regulatory 'break-outs' will see the compliance burden increase in the future. It will also (inimically) increase as unnecessary specific consumer regulation is repealed (see below) and the generic law becomes the sole means of protecting consumers in a wider range of areas. "[56] [Emphasis added]

[55] Productivity Commission "Review of Australia's Consumer Framework" Final Report- (30 April 2008) Australian Government Canberra Vol 1, p.19
[56], Productivity Commission "Review of Australia's Consumer Framework" Final Report- (30 April 2008) Australian Government Canberra Vol 1, p.19

- Option A - implements MCCA & COAG Recommendations

In May 2008, the Ministerial Council on Consumer Affairs (MCCA) and the Council of Australian Governments (COAG)[57] took the significant step to resolve to develop *national generic* unfair terms legislation to apply to all standard form consumer contracts.[58]

This was a significant step towards market. At no point did the Joint Communiqué foreshadow or acknowledge by COAG or MCCA the necessity for a 'regulatory breakout' from the operation of those laws for insurance policies.

In one sense, the commitment to the principles of a national generic unfair terms legislative platform acknowledges that there are sound economic and ethical reasons for all business to trade on fair terms.

The *Australian Consumer Law Bill*, now enshrined in substantively identical provisions in the *ASIC Act* and the *Trade Practices Act*, is a very positive benefit for consumers and the economy, and upholds the key recommendation of the Productivity Commission for national generic unfair terms legislation.

It is difficult to see how Options B, C and D, which provide for special treatment for the insurance industry above all other industries amounts to sound social policy. There does not appear to be any commercial or legal imperative to set apart this industry from any other in this area of consumer protection[59].

NLA suggests that there would be considerable economic and social costs in implementing compromise positions, which Options B, C or D represent, into a market where there is clear evidence of contracting on unfair terms. Consumer groups, regulator organisations and interested stakeholders have raised these concerns with insurance markets for some time, without satisfactory resolve.

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[57] Ministerial Council on Consumer Affairs Communiqué (23 May 2008)

[58] Subject to constitutional limitations outlined in Productivity Commission Recommendation 4.1

[59] Insurers enjoy healthy profit margins and have done so for some time. According to APRA statistics, for the period ending March 2008, the 113 Australian general insurance companies (direct insurers not reinsurers) had:

- total assets of $81.7 billion and total liabilities of $58.8 billion
- net premium revenue of $21.2 billion and net incurred claims of $13.8 billion

total underwriting expenses of $5.9 billion.

Ongoing consumer concerns with the insurance market include:

- Underinsurance

Australia faces a real and concerning issue regarding widespread underinsurance[60], particularly for the socially and economically disadvantaged[61]. The problem of underinsurance has in fact been a concern in the Australian community for some time. Most notably, ASIC produced a landmark report in 2005, arising out of its investigations into the devastating Canberra bushfires,[62] alerting the Australian community to the issue. Yet despite ASIC warnings and ongoing consumer concerns in the years that followed, the issue of underinsurance has never been properly resolved. Not surprisingly, the issue arose again most recently when it was calculated that some 25% of all people affected by the Victorian bushfires were actually uninsured.[63]

- Concerns with General Insurance Code of Practice and access to EDR

The General Insurance Code of Practice has come under increasing concern by the consumer sector for its lack of transparency in public reporting[64], failure to address consumer concerns in relation to problems with industry-wide multi-tiered Internal Dispute Resolution (IDR) processes[65] which have led to excessive delays in resolution of disputes, lack of fairness in outcomes for some consumers and difficulties in accessing Financial Ombudsman Service to resolve disputes. Criticism has also been made of the failure of the General Insurance Code to improve its provisions in relation to financial hardship, given the ongoing documented impact this has on our client base, the socially and economically disadvantaged.

Many of the these concerns have been relayed to industry over a number of years, but more recently were specifically put to the 2009 Review of the General Insurance

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[60] See for instance 'Underinsurance: A Case of Moral Hazard' by Professor Deborah Ralston
Acting Director, Melbourne Centre for Financial Studies
[61] See for instance Brotherhood of St Laurence's Report, 'Risk and Reality: Access to general insurance for people on low incomes', June 2006
[62] Australian Securities and Investments Commission, *Getting Home Insurance Right: A report on home building underinsurance*, Report No 54 (2005)
[63] See for instance 'Underinsurance: A Case of Moral Hazard' by Professor Deborah Ralston
Acting Director, Melbourne Centre for Financial Studies
[64] Up until 2008, Annual Code of Practice Reviews (which were historically contained in annual reports of Insurance Ombudsman Service), detailed the number of refused claims in general insurance, the number matters taken to Internal Dispute Resolution and the number of matters at EDR. Without current reporting of these statistics it is extremely difficult to determine the extent of the problem in relation to refused claims as well as barriers to access to EDR.
[65] See, for example, Submission responding to Issues Paper on the Independent Review of the IOS, Legal Aid NSW, May 2005

Code of Practice, in a Joint Consumer Submission.[66] Despite these key consumer concerns, the final report to the 2009 Review did little to address these concerns, particularly as they related to disadvantaged consumers.[67]

- Concerns with the Insurance Contracts Bill 2010

Consumer groups have recently expressed concern with the Insurance Contracts Bill 2010. These concerns were raised in a Joint Consumer Submission[68] into the review of the Insurance Contracts Act. As outlined in that submission, we foresee significant consumer risk on the current drafting on s 29, as well as a failed opportunity to improve the consumer position on s 31, s 56, s 35 and new electronic communication provisions - many of which were first identified in the 2004 Cameron Review as in need of improvement.

Given these unresolved consumer protection issues, it is critical that Option A is enacted. Option A is also the only effective way to ensure the protection of consumers of insurance products is aligned with protection of consumers in other financial markets (as envisaged by the Productivity Commission).

- Option A - Implements Senate Economics Committee Recommendations

In September 2009, the Senate Economics Legislation Committee reported on the necessity for implementing unfair terms legislation in insurance contracts. It took oral and written submissions from various industry and consumer groups and the regulators before recommending that:

> 'consumers are not provided with adequate protection in insurance contracts under existing law.'[69] (**Recommendation 2 at [10.12]**)

The Senate Economics Committee foreshadowed that the key challenge would be to ensure that any legislative reform - whether contained in the *Australian Consumer Law* or the *Insurance Contracts Acts* - must guarantee the 'equivalent level of

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[66] Joint Consumer Submission to the Review of General Insurance Code of Practice, ILS, July 2009
[67] See Report on the Independent Review of the General Insurance Code of Practice, R Cornall, 2009
[68] Joint consumer Submission to the Review of the *Insurance Contracts Bill* (2009)
[69] Senate Economics Legislation Committee Report, *Trade Practices Amendment (Australian Consumer Law) Bill 2009*, September 2009, p.68 Recommendation 2, 10.12

protection'[70] be provided to consumers in insurance contracts as any other consumer contracts (**Recommendation 2 at [10.13]**) Options B, C and D clearly offend the key recommendation of the Senate Economics Committee because Options B, C and D entail there being a 'special' status given to insurance.

When the Senate Economics Committee later observed (**Recommendation 2 at [10.14]**) that consideration needed to be given as to whether that legislation was contained in the *Australian Consumer Law* or the *Insurance Contracts Act*, that comment was made subject to the earlier commitment in **Recommendation 2 at [10.13]** an 'equivalent level of protection' be guaranteed for consumers. We are concerned that Options B and C are not the type of legislative response that the Senate Economics Committee had in mind when it referred to amendment to the *Insurance Contracts Act* as an alternative to amendment of *Australian Consumer Law*, because these options represent the 'regulatory breakout' warned against by the Productivity Commission and are not an equivalent level of protection as required by **Recommendation 2 at [10.13]**)

In our submission Options B, C and D cater to the public resistance by the insurance industry to commit to providing the same level of protection for consumers from unfair terms, as articulated by industry before the Senate Economics Committee[71], which will ultimately lead to a lack of *consumer confidence* and a fundamental failure of the *fair market* philosophy

- Option A - Represents 'Good consumer policy'

The Productivity Commission specifically quantified the economic and social value of *good consumer policy* to the Australian economy, when it stated:

> "*Good consumer policy* …activates the benefits of competition, contributing to greater product variety, higher firm efficiency and most importantly an impetus for innovation and productivity."[72] *[Emphasis added]*

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[70] Senate Economics Legislation Committee Report, *Trade Practices Amendment (Australian Consumer Law) Bill 2009*, September 2009, p.68 Recommendation 2, 10.13

[71] ICA oral and written submissions to Senate Economics Legislation Committee, *Trade Practices Amendment (Australian Consumer Law) Bill 2009,* , (Hansard) 26 August 2009

[72] Productivity Commission "Review of Australia's Consumer Framework" Final Report- (30 April 2008) Australian Government Canberra, Vol 2 at p.328

Option A meets this definition as it is the only option that implements:

1. Productivity Commission Recommendations;
2. COAG & MCCA Recommendations; and
3. Senate Economics Committee recommendations

We note, with some concern, that Table 1.2 of the Options Paper, which provides a 'preliminary impact assessment' of Option A, fails to calculate, in any respect, the significant benefits to consumer, government or indeed industry of implementing key expert and independent recommendations.

Additional comments - Response to Consultation question 5 (Option A)
The case for the need to implement Option A is compelling and as a suitable proposal for Australian consumers, is without rival in the Options Paper.

Details of Option A proposal

We make the following further comment on the mechanics and feasibility of implementing Option A. We also address and respond to purported industry concerns in respect of Option A.

- Amendment s 15 Insurance Contracts Act
We recommend an amendment of s 15 of the *Insurance Contracts Act*, to permit unfair terms provisions in the *ASIC Act* to operate in addition to and alongside the *Insurance Contracts Act* remedies. As we outline in this submission, such consequential amendment was always intended by the Productivity Commission, COAG and the MCAA as the crucial and necessary consequence on enacting generic, national unfair terms legislation.

- Third party beneficiaries
We support the suggested amendments to the *Australian Consumer Law* to clarify that the legislation is intended to apply to third party beneficiaries. This could be achieved quite easily. Such a legislative framework already exists in NSW under the *Consumer Claims Act*, where it is clear that a third party beneficiary has standing to

make a claim in respect to the provision of goods or services.[73] That framework is relevant to this discussion because it demonstrates in practical terms that extending *Australian Consumer Law* to accommodate third party beneficiary claims merely reflects the modern day reality that many consumers receive benefits beyond the technical confines of privity of contract.

- Main subject matter exemption s 5

For the reasons outlined below (see **Part 2** - *'Industry concerns over Option A - Supposed 'special' nature of insurance '*), s 5 of the *Australian Consumer Law* ought to be amended to specifically acknowledge that, in respect of insurance contracts, a term which seeks to limit or exclude liability is not caught by the main subject matter exemption (and as such is caught by the unfair terms provisions).

Indeed, given the ease upon which the *Australian Consumer Law* should be able to be appropriately amended to accommodate third party beneficiaries, further supports the viability of Option A as the only appropriate proposal for implementation.

- ASIC Powers

A key benefit to consumers and the community at large of the new unfair terms provisions is that they will provide ASIC with new powers to intervene in a fair but effective way. Consumer submissions to the Senate Economics Legislation Committee and consultation papers on the implementation of national generic legislation to regulate unfair terms, have documented in considerable detail the significant benefit to consumers of having a regulator that efficiently but reasonably negotiates around unfair terms. Industry concerns that the new regime would disrupt business have simply not been borne out in practice in UK or Victoria, where regulator intervention has worked without significant concern for some considerable time.

The great strength of this legislation, as borne out in the UK and Victorian experience, is that regulator intervention is usually targeted in respect of relatively minor but widespread harm. The regulator clearly feels comfortable exercising its powers because the remedy is a proportionate and measured response. Unlike intervention which provides a basis to strike down contracts, a key focus of these

[73] s 3 *Consumer Claims Act* (NSW) 1998 - definition of "consumer" extends to a person who received goods or services whether or not they are provided under contract.

provisions is simply, through negotiation (rather than litigation) to encourage traders to redraft harsh contract provisions that offend unfair terms legislation.

We support the comments of the Minister in this regard, where he noted in respect of the recently enacted *Australian Consumer Law* unfair terms provisions:

> Redress for non-parties will allow the ACCC and ASIC to act more effectively where, for instance, thousands of consumers suffer small losses on which each of them might not take action individually because of cost and inconvenience. Businesses should not profit from consumer detriment, just because the amount is small or the harm is spread widely. This is not a general power to award damages, but a power to order redress where that loss or damage is clearly identifiable and there is no need to decide the merits of each case. It could be used to order redress such as an apology, the exchange of goods or a refund. [74]

Industry concerns over Option A

The concerns raised by industry as the basis for rejecting Option A in our view lacks the credibility of proper analysis. At its highest, insurers say that unfair terms legislation in Australian Consumer Law would create "increased complexity of regulation" and the costs associated with dual pleadings.

NLA submits that if this represents the greatest concerns industry has with committing to unfair terms legislation then:

1. Industry has not nearly met the evidential burden it carries[75] of establishing why it should *not* enact the *Australian Consumer Law*;

2. Treasury has sufficient information before it to be comfortable that the cost of regulatory compliance with *Australian Consumer Law* does not outweigh the benefit of introducing the legislation.

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[74] Hon Dr Craig Emerson, Second Reading Speech, House of Representative Hansard, 24 June 2009, p.6988

[75] The Senate Committee expressed the clear view that given the weight of evidence establishing the existence for unfair terms, it would be on those would opposed the introduction of such laws to make the case against unfair terms legislation: Senate Economics Legislation Committee, *Trade Practices Amendment (Australian Consumer Law) Bill 2009*, Recommendations at para 10.11

- Generic legislation overlaying industry specific legislation

The notion that overlaying generic legislation over industry-specific legislation creates a proper basis for rejecting the generic legislation is not a new nor novel concept in this debate. The Productivity Commission heard and rejected such claims when it ultimately recommended national generic unfair terms legislation. Equally, such concerns were raised[76] but ultimately rejected by the Senate Economics Legislation Committee as a basis for not enacting overlaying unfair terms provisions.[77]. Other (significant) industries that will be subject to industry-specific legislation and *Australian Consumer Law* include other financial service providers such as the banks, energy services and telecommunications industries. We see insufficient evidence to support a regulatory breakout for insurers.

Moreover, where the generic legislation complements the industry-specific legislation, we see a net regulatory benefit for the Australian community. For the reasons we outlined above in respect of ASIC powers, the enactment of unfair terms regulation will ensure that the provisions relating to good faith are ultimately complied with.

- Dual pleadings

The argument that the purported cost of drafting dual pleadings is a proper basis for not enacting unfair terms legislation does not have any substance. Insurance claims are initiated by consumers not insurers and as noted above, few consumers are able to mount legal challenges against refusals. Hence the increased cost to insurers in this regard would be negligible.

In any event, dual pleadings represent the reality for litigation in most jurisdictions in this country and it would not be uncommon for an insurance pleading to be a dual pleading that pleads the common law, *ASIC Act* and (to a lesser extent) *Corporations Act*.

Finally, concerns regarding dual pleadings reflect a broader argument that insurers have run for some time in this debate - namely, that the *Insurance Contracts Act* is, in one form or another, a self-contained code. For the reasons we outline in some

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[76] ICA oral and written submissions to Senate Economics Legislation Committee, *Trade Practices Amendment (Australian Consumer Law) Bill 2009*, (Hansard) 26 August 2009, p6

[77] See Recommendations at para 10.12 - 10.14 Senate Economics Legislation Committee, *Trade Practices Amendment (Australian Consumer Law) Bill 2009*,

detail in **Part 2** below (see **Additional comments** in **response** to **Consultation Question 4 & Question 5)**, this is a significant misconception of the operation of *Insurance Contracts Act* as it is rather, complimentary legislation to the common law and other statutory regulation.[78] Indeed the notes to the draft Insurance Contracts Bill state:

> 'The Insurance Contracts Act is not a code of insurance contract law. It only relates to certain aspects of the law relating to insurance contracts.'[79]

This view has since been confirmed by the High Court in *Akai Pty Ltd v People's Insurance Co* (1996) 188 CLR 418 at 432, where the Court said of the *Insurance Contracts Act*:

> "The function of s 7 is to confirm that the statute is *not* a code of insurance contract law and that, rather, it *only relates to certain aspects of the law relating to insurance contract*." [Emphasis added]

- Supposed 'special' nature of insurance

Finally, an underlying theme being provided as a basis for considering the regulatory breakout articulated in Options B & C and the rejection of Option A, is the notion that insurance contracts are somehow 'special' in that 'the contract for the product and the product itself are one and the same thing' (see paragraph 29 of the Options Paper) – and that therefore insurance would be excluded from unfair terms legislation under the main subject matter exemption.

NLA submits that the notion of a 'special' position for insurance in the market is based on a fundamental misunderstanding as to the nature of insurance contracts and the operation of the unfair terms provisions in the *Australian Consumer Law* to the insurance market.

Author Greg Pynt describes the nature of insurance as "an insured transferring to an insurer the burden of any financial loss the insured might suffer if the event specified in the risk transfer arrangement between the insurer and the insured fortuitously occurs during the period of the arrangement".[80] There is no reference in this

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[78] s 7 *Insurance Contracts Act*.
[79] P Mann, Annotated Insurance Contracts Act, 4th Ed at p
[80] G Pynt Australian Insurance Law, First Ed, Butterworths, 2008 at p. 2

definition to insurance as a product that is defined by what it is *not* – put differently, insurance as a product is not a negative construct. Insurance is a positive financial product that offers the transfer of risk for consumers in relation to key financial assets and events that affect them - their home and contents, their motor vehicle, their travel and the like.

A key feature of *Australian Consumer Law* unfair terms legislation is that it draws from common law concepts such as *protection of legitimate business interest*. We submit that statutory intervention that pays respect to classic common law theory is highly beneficial to the Australian economy in that it provides market certainty by developing well-known and clearly defined common law principles.[81] The *Australian Consumer Law* fairly but proportionately extends the reach of the law slightly further to provide relief where it would be unconscionable for insurers to benefit over the long term by drafting exclusion clauses on unfair terms.

To ease industry concerns however, we quite rightly acknowledge that consumer relief for breach of unfair terms is not and should not be open-ended. Where an insurer can objectively demonstrate that the term was *necessary to protect their legitimate business interests*, no consumer relief will be granted. This concept, of calling upon an insurer to provide some evidence to substantiate a proper basis to refuse a consumer claim which they can demonstrate relates to their bottom line, is not a new concept. In different ways, provisions such section 28, 29 and (even) s 54 *Insurance Contracts Act*, to one extent or another, already require a similar exercise to take place - but obviously in respect of very different matters to the operation of unfair terms legislation.

It is clear from what is said above that a Court or regulator would, in our view, have no trouble in identifying, on the basis of applying existing unfair terms laws, those particular terms in a properly drafted insurance policy which would be the subject for review - i.e. exclusion clauses or clauses which limit liability - from the key provisions that define the subject matter of the policy, which is not subject to review.

In this sense Option A promotes good policy drafting, adherence to existing commitment FSR reforms for insurers' PDS', pays due deference to classic contract

[81] See for instance, Submission to Treasury re Australian Consumer Law, Legal Aid NSW, June 2009

law theory and should, by all accounts, stabilise the market in the process by creating confident consumers and fair markets.

To avoid any doubt as to the proper operation of the main subject matter exclusion to insurance contracts, it is recommended that an amendment be made at s 5 of the *Australian Consumer Law* as set out above. Such limiting liability clauses would ordinarily include exclusion clauses but may also relate in insurance contracts to meeting certain condition precedents before cover is said to apply or purported defining cover by a description of what it is not (eg: Travel policies are notorious for limiting cover in respect of certain 'defined events' - which are in fact limitations on the cover).

- *The case against implementing Option A has not been made out*

As the Senate Economics Legislation Committee rightly pointed out in its recommendations on the implementation of unfair terms legislation, that given the weight of evidence it received on unfair and harsh terms in insurance contracts, the onus must be on those who do *not* believe these provisions should cover insurance contracts to prove their case.[82] Clearly, this has not been achieved and the case *against* Option A has not been proved.

[82] Senate Economics Legislation Committee, *Trade Practices Amendment (Australian Consumer Law) Bill 2009*, Recommendations at para 10.11

Part 3 - Response to 'regulatory breakout' proposals
(Options B, C & D)

Given the scope of the problem outlined in Part 1, any legislative response must meet the government's key objective - being to prevent consumers (including third party beneficiaries) of standard form insurance contracts from suffering detriment due to terms in the contract that are unfair or harsh.[83]

As NLA and other key consumer stakeholder organisations[84] maintain in response to the Options Paper proposal, Option A is the only viable and appropriate legislative response that is guaranteed to achieve the government's key objective of removing consumer detriment. The arguments as to why Options B and C are not equally viable options are outlined in Part 2 above.

We provide the following further comments in response to Options B, C and D, which demonstrate the significant regulatory breakout and accompanying risks to the Australian economy that such proposals would bring.

- Response to Consultation question 6 (Option B)

Option B represents a regulatory breakout in that it is clear that what is intended to be achieved is a modified version of unfair terms legislation that takes into account industry's argument the 'special' status of insurance. Whilst the proposal subject heading to Option B in the Options Paper advises that the proposal is to 'extend *Insurance Contracts Act* remedies to include unfair contract terms provisions' the detail of proposal is much more alarming. The proposal includes considering:

1. Limiting the reach of unfair terms provisions to only 'some categories of terms'[85]
2. Permitting insurers to continue to trade on unfair terms in respect of the main subject matter, which would include provisions on cover and the limits on cover[86]

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[83] Treasury 'Unfair Terms in Insurance Contracts - Options Paper' p. 6
[84] See for instance Submissions by Consumer Action Law Centre to Treasury 'Unfair Terms in Insurance Contracts - Options Paper' May 2010, instance Submissions by Insurance Law to Treasury 'Unfair Terms in Insurance Contracts - Options Paper' May 2010
[85] The Options Paper provides no further details of what this would entail. See p.10 at para 27
[86] Treasury 'Unfair Terms in Insurance Contracts - Options Paper' May 2010 at p.10 para 29

3. Focusing on developing new remedies in the *Insurance Contracts Act* only around the fairness and transparency of exclusions from cover.[87]

Option B does not resemble unfair terms legislation as is currently enacted in the *Australian Consumer Law*. Without the ability of consumers to have a right of redress in relation to unfair definitions of cover (or more correctly described earlier in this submission as *non-cover* cover) or providing substantive redress for consumers on clauses with seek to limit or exclude liability, there will be little point in enacting such legislation. NLA therefore does not support Option B as a realistic and viable proposal that meets the government's key objectives for this legislation.

Realistically speaking, Option B will permit insurers to continue to trade on unfair terms with some minor patch-up provisions being developed around the transparency of exclusion clauses. This does not get to the heart of the issue for consumers as outlined in Part 1 above and will not lead to any real change in market behaviour that the Productivity Commission had cost-assessed.

The regulatory breakout that Option B (and Option C) necessarily entails will also bring with it whole new sets of concerns around new hybrid laws that have no basis in common law, remain un-costed and where there is no history of enforcement around such terms. Such hybrid laws brings huge regulatory costs and a level of uncertainty to the markets as Courts or Financial Ombudsman Service will have difficulty in understanding the parameters of that new body of law. Those inherent costs and the risks of Option B are not properly outlined in the Preliminary Impact Assessment summary (Table 1.3).

Additional comments - Response to Consultation question 7 (Option C)
For the reasons outlined in **Part 1** and **Part 2** above, Option C is rejected as a viable response to consumer detriment in that it does not meet the key objective of government to remove consumer detriment in respect of harsh or unfair terms in insurance policies. Option C represents a regulatory breakout of some considerable proportion in that it would be seeking to use existing principles such as good faith as a basis for striking down unfair terms.

[87] Treasury 'Unfair Terms in Insurance Contracts - Options Paper' May 2010 at p.10 para 29

As outlined in **Part 1** and **Part 2** above, utmost good faith has a troubled history as a tool which provides enough clear guidance as a basis for relief, particularly in respect to harsh or unfair terms. The fact that in the last three decades, there have been extremely few cases which have considered good faith as a principle and the very modest number of cases decided at Financial Ombudsman Service on utmost good faith is telling in this debate as to the lack of potential of this principle to provide the legal certainty needed in this area. Author Matthew Ellis notes the jurisprudence around utmost good faith is limited, quite possibly because of difficulties defining what it is. He states::

> "Defining utmost good faith and specifying the standard of conduct required to be met by parties under a policy of insurance has proved to be difficult. In this regard, the development of jurisprudence around the duty of utmost good faith since the enactment of the ICA has been slow, with greater advancement in the understanding of the duty coming through commentators such as Tony Scotford, Fred Hawke and Kenneth Sutton than through judgments delivered in Australian law courts* [*See, eg, T Scotford, 'The Insurer's Duty of Utmost Good Faith, Implications for Australian Insurers' (1988) 1 *ILJ* 1 (being the first substantive analysis of the concept of utmost good faith under the ICA in Australia); F Hawke,'Utmost Good Faith — what does it really mean?' (1994) 6 *ILJ* 91 and K Sutton, *Insurance Law in Australia*, 3rd ed, LBC Information Services, 1999, pp 157–63.][88]

Given the troubled history of utmost good faith in a jurisprudence sense, we foresee considerable risk to both consumers, industry, the regulator and the insurance market generally if Option C was enacted. For this reason we firmly reject Option C as a viable alternative.

Additional comments - Response to Consultation question 8 (Option D)
Given the clearly identified problems with unfair terms in insurance contracts and consumer concerns with the insurance market generally (**Part 1**), and the viability of implementing Option A to insurance contracts (**Part 2**), we see no proper basis upon which industry has established a case for a regulatory break –out and consequentially self-regulation in this area.

[88] 'Utmost Good Faith: The scope and application of s 13 of the Insurance Contracts Act in the wake of CGU v AMP' (2009) 20 ILJ 92

Thank you for the opportunity to provide these comments.

Should you require further information, please feel free to contact Louise Smith, Executive Officer on (03) 6236 3813 or by email to louise.smith@legalaid.tas.gov.au.

Yours sincerely

Alan Kirkland
Chair

Appendix 1

Commentary from Insurance Ombudsman on determinations - harsh/unfair terms issues

2006-2007 IOS Annual Review

Panel Report

'Rubbery' policy terms

"The Panel has also considered a number of policies which include terms best described as "rubbery". They contain "open-ended" or vague exclusions or clauses which make the commencement or operation of the policy dependent upon external factors. One example of a rubbery policy is the type of travel policy which has an open-ended class of persons whose illnesses are excluded from policy cover if they cause cancellation of the journey. An example of a rubbery clause is a policy exclusion entitling an insurer to deny a claim if the illnesses causing cancellation of the journey is due to (after listing specific classes of persons) "any other person on whom your trip depends". The Panel has found that such a clause gives an insurance company a huge discretion to apply the exclusion. Does it mean the tour operator, the financier, the guide for a trekking or cycling holiday, the skiing or diving instructor, or some distant relative whose sudden death results in the command to return immediately for the dignity and honour of the family?"[89]

2005 IOS Annual Review

Panel Report

"The Policy Terms

Now we come to the substantive terms of the policy, many of which are not in the policy document. For example, they may be found in the policy schedule or the policy certificate or in a separate letter providing special policy terms, or in a brochure or a PDS, which may or may not be part of the actual policy, or in a derogation notice (which, sadly, we do not see many of these days).

In some instances, part of the policy term might be in the policy, and another part may be in the schedule or the certificate. In these circumstances, it is important the documents speak to one another.

[89] 2006-2007 Insurance Ombudsman Annual Review, p.19

This problem arose in Determination No. 20276 when the Panel had to consider whether the insurer had met its obligations to clearly convey a crucial limitation of cover – namely that it only covered drivers 30 years and over. The applicant brought a claim for damage to her motor vehicle when it was involved in an accident while being driven by her 20-year-old daughter. At the time when she took out the policy, there were no persons likely to drive the vehicle who were under the age of 30. However, subsequent to that time, her daughter obtained her licence and the applicant allowed her to drive the vehicle on the day of the accident. The policy schedule provided by the insurer at the time of policy inception included the following:

> "Comprehensive cover – provides cover for:
> • Certain optional covers (where agreed) such as rental or loan car following an accident, removal of basic excess for windscreen claims, protected no claim bonus and restricted driver cover.

Note that the restricted driver option provides a discounted premium, but limits the drivers who are covered under the policy."

It then set out a number of policy excesses including:

> "Inexperienced Driver Excess $600
> Undeclared Young Driver Excess $900"

The inexperienced driver excess was said to apply to drivers over the age of 25 who had held their Australian driver licence for less than two years and the undeclared young driver's excess applied to drivers under the age of 25 years not listed on the policy schedule.

The applicant, not surprisingly, on reading this document thought her daughter was covered although she expected to pay an additional excess.

However, the policy document provided something else which the applicant said she did not expect. On page 11 of the policy, under the heading "Restricted Drivers", the following appeared:

> "When the current schedule shows that the restricted driver option applies, we will not cover any accidental loss, damage or liability, which results in a claim, when the driver of your vehicle was a person under 30 years of age."

The product disclosure statement contained in the introduction to the policy document provided no such exclusion, although it did state:

> "Note that the restricted driver option provides a discounted premium, but limits the drivers who are covered under the
> policy."

The policy contained an index which includes "Words with Special Meanings" on page 4, and while there were two types of driver descriptions in this section of the policy and a special meaning was given to them, there was no definition therein of the word "restricted driver". In the course of its determination, the Panel made the following comments:

> "… an insurer must take great care to make sure its procedures for selling the policy and the documentation it produces thereafter is expressed in the clearest possible terms.
>
> After all, the obligation is to act with the utmost good faith, not simply good faith, which is a heavy onus in this context on an insurer;" [Emphasis added]

The fundamental principle relevant to all insurance disputation on which all parties agree is that no-one ever reads the policy before a claim is made. This is always how it has been and probably will be. Most people read mortgage documents, loan agreements, leases, contracts for the purchase of motor vehicles, even rate notices, but they will not, or maybe cannot, read an insurance policy."[90]

[90] 2005 Insurance Ombudsman Service Review, Addendum at pp 3 - 4

2004 IOS Annual Review

Panel Report

[Referring to 4 determinations before the Panel Chair in travel insurance, motor vehicle insurance, landlord insurance and total and permanent disability, which are outlined in Insurance Law Service submission[91] to the Senate Inquiry]

"In his report, the Panel Chair, Peter Hardham, illustrated a number of instances where the Panel has made decisions which, whilst legally correct, may be viewed as unfair or harsh. This raises the question as to whether there is more law than justice in some areas of insurance law and practice. In other words, does the law produce results which the community might regard as providing an unjust result?"[92]

2003 IOS Annual Review

'Claims Review Panel Report – The Illusory Nature of Cover'

[The Panel referred to Determination 15669 in respect of a home and contents policy, an insurer rejected a claim for damage caused by leaking pipes on the basis of an exclusion clause which broadly defined damage to include "no matter how caused". The issue was that earth movement will in such circumstances occur and that movement may be caught by such a broad exclusion.]

"The point we want to make in dealing with this dispute is that we believe cover contained in an insurance policy is indeed illusory, if the very event giving rise to the claim, for which cover is provided, is likely by virtue of a process of cause and effect to give rise the the circumstances covered by a policy exclusion, particularly where the policy exclusion is in a separate part of the policy."[93]

1999 IEC Annual Review

'Claims Panel Review Report '

"Of course there are many different definitions of flood, some narrow and some wide. In one instance the Panel was dealing with a policy where flood was defined as

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[91] Insurance Law Service Submission to Senate Inquiry into Australian Consumer Law Bill (2009),p 3-4

[92] 2004 Insurance Ombudsman Service Annual Review, p.25

[93] 2003 Insurance Ombudsman Annual Review, p.28-29

including water that escaped not only from a natural or artificial watercourse, it also included water discharged from sewerage systems by the general pressure induced by floodwater, and to our surprise, it also included "general run-off that comes from any area outside the building". [94]

1998 IEC Annual Review

Claims Panel Review Report
'Unusual Provisions'
[The Claims Review Panel considered various examples in insurance contracts of unusual provisions and noted that insurers had failed to comply with their obligations to advise insureds of unusual terms in their policies under s 35 and s 37.]

"In Determination D, the Panel had to consider a claim under a policy that provided 'we will not pay for any loss by theft unless there is forcible entry to your building'. This was not an unusual clause, but what caused the problem was the expression 'forcible entry' was specially defined in the policy to mean 'Forcible entry means the unauthorised forced entry of your building which causes physical damage to your building at the point of entry. This definition imposed a much wider meaning to the term 'forcible entry' as imposed by the Courts and constituted a much wider exclusion than that contained in Standard Cover."[95] [Panel's emphasis]

1993 IEC Annual Review

Travel Insurance – case study
"Ms F returned home from overseas to be at her mother's sick-bed. She thought that she was covered for the cost to resume her trip but found that because more than 50% of the trip had elapsed, she was not. The policy wording made this clear but the promotional part of the brochure – where the benefits are highlighted – described the benefits to include 'Free flight return overseas to continue your journey if disrupted. The qualification was made, but not in an equally prominent fashion."[96]

[94] 1999 Insurance and Enquiries and Complaints Ltd p.9
[95] 1998 Insurance and Enquiries and Complaints Ltd, p. 9
[96] 1993 Insurance and Enquiries and Complaints Ltd, p. 10