QBE Submission

Quality of Advice Review

7 June 2022

About QBE

QBE Insurance Group Limited is an international insurer with insurance products covering a diverse portfolio including property, crop, energy, marine and aviation. Headquartered in Sydney and listed on the Australian Securities Exchange, we employ more than 11,700 people in 27 countries around the world.

QBE Insurance (Australia) Ltd (QBE) has offices in all Australian states and territories and provides a broad range of general insurance products to personal, business, corporate and institutional customers.

Since its origins in Queensland over 130 years ago, QBE has been an integral part of the Australian business landscape, providing peace of mind to Australians during normal business and times of crises.

QBE is proud of its heritage and the support that it has provided to our customers and policy holders during this time. Our purpose – enabling a more resilient future.

Contents

Overview 4
General observations 4
Specific considerations 5
Intermediated insurance distribution 5
Competitive effects and considerations 8
Conclusion 10

Overview

On 11 March 2022, the Government released terms of reference for the Quality of Advice Review (***Review***). The Review is being undertaken by an Independent Reviewer, with a final report due to Government by 16 December 2022.

The Review is to address Recommendations 2.3, 2.5 and 2.6 of the Financial Services Royal Commission (***FSRC***) focusing on the effectiveness of measures to improve the quality of financial advice. Recommendation 2.6 relates specifically to general insurance and is to consider whether the current exemptions for general insurance from the ban on conflicted remuneration remain justified.

The general ban on conflicted remuneration (including commissions, volume payments and soft-dollar benefits) was introduced by the Future of Financial Advice (***FOFA***) reforms in 2013. The purpose was to remove any conflict that may arise between advisers and their clients' interests when advisers are provided with incentives from the issuers of financial products. The intent was to ensure advisers were free to act in the best interests of their clients and provide better quality advice.

The FOFA reforms also provided certain exceptions from the general ban, including general insurance products and consumer credit insurance products. Monetary and non-monetary benefits given solely in relation to these products are currently wholly exempt from the ban.

On 24 March 2022, an Issues Paper was released for consultation as part of the Review. QBE welcomes the opportunity to provide feedback on the Issues Paper. QBE has worked with the Insurance Council of Australia (***ICA***) and supports the ICA's general insurance industry submission on the Issues Paper (***ICA submission***). Our comments below provide supplementary information from a QBE perspective specifically in relation to the current general insurance exemption from the ban on conflicted remuneration.

General observations

General insurance is a fundamental foundation of a modern economy and touches almost all levels of the community and our individual human and corporate activities. A strong, stable, competitive and innovative insurance industry, with accessible and affordable products for businesses, communities and governments, is critical for the smooth functioning of the economy.

Regulatory regimes can either enable or impede a competitive and innovative insurance sector. Insurers need to be able to cover costs and provide appropriate returns to shareholders to attract investment capital. Conduct of insurers is also vital to ensure that as an industry, we build and maintain trust, we are truly customer focused, and we address any issues as they arise. QBE considers it is important to find the right balance between stability and protection on the one hand, and national competitiveness and productivity on the other.

In relation to conflicted remuneration, initial industry discussions with the Independent Reviewer indicate the starting point for the Review is consistent with the proposition posed by Commissioner Hayne in the FSRC. That is, conflicted remuneration will always, by definition, raise the risk of poorer quality advice because it misaligns the incentives of advisers from the interests of consumers. Commissioner Hayne noted this is *"the unchallenged (and unchallengeable) basic premise for the conflicted remuneration provisions"*[1].

The Issues Paper raises the question: *"what would be the implications for consumers if the exemptions from the ban on conflicted remuneration were removed, including on the quality of financial advice and the affordability and accessibility of advice?"*. QBE supports consideration of this question, and also supports the overriding objective to protect consumers from harm. We would, however, be concerned if the Review considered this question in isolation and urge the Review to also consider a range of broader policy objectives, such as:

- **Benefits to consumers** – the structure and availability of intermediated sales channels delivers accessibility, choice and other benefits such as specialist product and risk management advice. The impact on consumers of potential regulatory reform that may affect accessibility of insurance or result in insurers and intermediaries re-pricing, modifying or withdrawing their services should be carefully considered.

[1] FSRC, *Final Report*, Volume 1, February 2019, pp181–2.

- **Differing characteristics of intermediaries** – there are a range of insurance intermediaries operating in the market and they do not all function in the same way, for instance they may act on behalf of insurers or the customer. This distinction needs to be considered in the context of the role remuneration plays in the effectiveness of these distribution channels, including on the quality, affordability and accessibility of advice.
- **Competition and innovation** – intermediated sales channels also operate to facilitate competition and innovation in the general insurance market. It is critical that the regulatory regime does not favour one distribution model over another to create an un-level playing field. Reforms that inadvertently operate to reduce competition and stifle innovation will ultimately (if not in the short term) be detrimental for customers.

As outlined in the ICA submission, general insurance products are very different to the types of financial products that were identified as having caused significant consumer harm and were a key driver of the FOFA reforms. General insurance products are better understood by customers, are generally of 12-months duration, easily cancellable and insurers are subject to a duty of "utmost good faith". General insurance products were exempted from the FOFA reforms in recognition of these differences.

It is also important to understand that there is an overriding social (and economic) objective for the nation which is ensuring consumers can readily access suitable and affordable insurance products to protect themselves from harm and mitigate risk.

These matters also need to be considered against the backdrop of recent far-reaching regulatory reforms introduced by Government to strengthen the requirements applicable to the sale of general insurance and reduce the potential for mis-selling. Extensive new protections for consumers have been introduced to address identified instances of consumer harm, including design and distribution obligations, the prohibition on hawking, the deferred sales model for add-on insurance and the extension of the unfair contract terms regime to insurance contracts (further detail is included in the ICA submission). In addition, enhanced regulatory powers to improve consumer outcomes have been provided to the Australian Securities and Investments Commission (***ASIC***), including significant product intervention powers.

We strongly suggest there should be an opportunity for these significant reforms to be embedded and their effectiveness assessed prior to any further changes to the regulatory framework to minimise any unintended consequences.

Specific considerations

Intermediated insurance distribution

Insurance intermediaries are a critical component of the distribution chain for a significant number of Australian insurance providers, driving competition and innovation in the market. These distribution channels provide increased accessibility, choice and a range of additional benefits for customers. A large percentage of insurance policies in Australia are incepted through these channels. The ICA submission highlights a range of intermediated insurance distribution models currently operating in Australia.

We believe the role of remuneration in the effectiveness of these distribution channels, including on the quality of financial advice and the affordability and accessibility of advice, needs to be considered in the context of the broader competitive insurance market landscape.

We also recognise that intermediaries do not all function in the same way. There are different structural arrangements and characteristics, including differences in the interests for whom they act. The Australian Competition and Consumer Commission (***ACCC***) categorises intermediaries as "insurer intermediaries" and "customer intermediaries"[2]. These differences warrant consideration, as outlined below.

Insurer intermediaries

Insurer intermediaries conduct business as an agent, or on behalf, of insurers. They may operate exclusively for a single insurer or may be independent and work with more than one insurer. In most cases, an insurer

[2] ACCC, *Northern Australia Insurance Inquiry,* Final Report, November 2020 (***ACCC report***), p471. The ACCC also notes insurers may retain referral networks, with a specific type of referrer being comparison websites. These are not considered in detail here given they are not involved in directly arranging contracts of insurance.

intermediary will be required to hold an Australian Financial Services Licence (***AFSL***) or be appointed as an Authorised Representative (***AR***) of another AFSL holder such as an insurer[3].

Insurer intermediaries typically include:

- Distributors – for example, these may range from travel agents and real estate agents to car dealerships and furniture removalists to banks and other financial institutions (noting the insurance products being distributed may be either insurer-branded or 'white-labelled'); and
- Underwriting agencies – generally these are specialist agencies that focus on particular market segments or specialist insurance product lines. Underwriting agencies may distribute an insurer's products either directly to customers or through other intermediaries (such as insurance brokers).

The customer benefits provided by distributor insurance intermediaries are detailed in the ICA submission. In addition, the benefits of underwriting agencies include:

- Specialist product expertise – customers can access specialist advice and insurance products specific to their risks that may not be as widely available through other distribution channels. Insurers can also leverage this experience and expertise to develop and distribute suitable products to customers, without the need to develop extensive, and potentially costly, in-house skills.
- Geographical reach – where agencies focus on particular market segments. For example, they may be geographically established to service particular markets, such as in regional, rural or remote communities. Again, insurers can leverage these types of networks without having to establish their own local presence.
- Technology – with the continual growth in online platforms and digitisation, underwriting agencies are continuing to innovate and differentiate – not only in products and services, but in technology – integrating with insurer and broker networks, speeding up quoting and placement services for customers.

Case study – Elders Insurance

*Elders Insurance (Underwriting Agency) Pty Limited (**Elders**), is an underwriting agency and AFSL holder majority owned by QBE. Elders has a rich history supporting rural and regional Australians, providing insurance products that are designed to suit local conditions and circumstances.*

*Elders sells a range of personal, commercial and farm insurance products which are underwritten by QBE. Elder's appoints ARs to act on its behalf (**Elders ARs,** also known as **Elders Agents**) in the sale of insurance products. Elders Agents are independent franchisees with over 200 locations across regional and rural Australia, and also metropolitan areas.*

Elders sells insurance products:

- *by way of electronic quote and bind platforms which provide connectivity between QBE and Elders Agents;*
- *as a result of case by case negotiations between QBE and individual Elders Agents;*
- *in person; and*
- *over the phone.*

Elders authorises Elders Agents to provide general advice and personal advice to sell insurance products to customers. Elders Agents own the relationship with customers – QBE does not have a direct relationship with the customer during the sale of the product or any dealings with the customer for policy maintenance purposes.

QBE provides monetary benefits to Elders, including by way of commissions, because Elders Agents own the relationship with the customer and provide services to them. Elders Agents have overhead, staff and other costs associated with running their own franchise and providing services to customers purchasing insurance utilising Elder's placement services. We believe the commissions we pay to Elders reflect the effort required to place the business with QBE.

As an AFSL holder, Elders is subject to the regulatory regime administered by ASIC. Elders Agents are also monitored by QBE through a comprehensive quality assurance system, together with regular audits.

As outlined below, insurers incur acquisition costs for all forms of distribution, including through insurer intermediaries, and will remunerate insurer intermediaries for the agency and distribution services and benefits they provide.

On the issue of conflicted remuneration, Commissioner Hayne expressed the view that: *"sales staff can be rewarded by commission; advisers should not be"*[4]. The ACCC, in considering the effect of intermediary remuneration arrangements, noted the distinction between an insurer intermediary and an insurance broker

[3] The obligation to hold an AFSL or be an AR will depend on the nature of the conduct engaged in by the intermediary, for instance, providing referrals may not require an AFSL or AR relationship.
[4] FSRC, Interim Report Volume 1, September 2018, p98.

indicating *“[a]n insurer intermediary, by definition, should act on behalf of the insurer. In many respects they are akin to sales staff of an insurer. In most cases, an insurer intermediary will act on behalf of a single insurer.”*

Importantly, the ACCC did not recommend the exemption from the ban on conflicted remuneration be removed for insurer intermediaries, given their likeness to sales staff of insurers. QBE suggests the distinction between insurer intermediaries and consumer intermediaries is an important consideration in assessing the appropriateness of the ban. We also recognise there may be other relevant matters for consideration (for instance, if the intermediary does not act exclusively for a single insurer and the nature of the remuneration provided).

Consumer intermediaries

Insurance brokers act on behalf of customers, assisting to select and arrange insurance products. Brokers will often provide a range of additional services for customers including risk management advice and claims advocacy services. Brokers are AFSL holders.

A recent report prepared for the National Insurance Brokers Association (***NIBA***), details a range of benefits and value provided by brokers to their clients, to insurers and the economy and society more broadly, in summary[5]:

- For clients: Brokers facilitate the purchase of appropriate insurance on behalf of their client (the customer) and provide support throughout the insurance lifecycle, including general risk advice and claims advocacy.
- For insurers: Brokers support insurers to distribute products efficiently and effectively. Insurers can minimise their product distribution costs, access a greater range of clients, and support product innovation.
- For the economy: Brokers’ facilitation of insurance sales results in greater choice and competition in the insurance market, and more appropriate purchasing of insurance (i.e. reducing underinsurance or over-insurance), which promotes more efficient market outcomes.
- For government and broader society: Brokers support society to guard against risks, and manage the placement of risks between the client, the insurer and the government. In the absence of risk solutions provided by brokers, these incidents would take far longer for the economy to recover from, and there would be a greater cost borne by government.

Case study – Broker networks[6]

The insurance broker market in Australia is predominantly made up of hundreds of small, privately owned brokerages. However, many of these small businesses join an insurance broker network, to access the benefits of size and scale. Networks provide brokers with enhanced buying power and scale which allows them to better negotiate policy terms and conditions with insurers. This supports greater choice for clients, as brokers work with their network to access customised and tailored products.

Brokers’ alignment to a professional network also provides benefits to the insurer. Networks represent a single point of contact for an insurer to access a large distribution channel in a fragmented market. Brokers use networks to share product and insurer information and to negotiate policy terms, creating an efficiency for the insurer by reducing the number of points of contact from individual brokers.

As with insurer intermediaries, insurers will provide remuneration, such as commissions, to insurance brokers for the distribution services and benefits they provide.

As outlined by the ACCC[7], an insurance broker owes their primary duty of care to the insured, as principal. In addition, as AFSL holders, insurance brokers are required to do all things necessary to ensure that their services are provided efficiently, honestly and fairly. The ACCC noted this duty to the consumer should prevail even though an insurance broker may have remuneration arrangements in place with a number of insurers, however recognised *“there is clearly a much greater potential for an insurance broker’s remuneration arrangements with insurers to lead to a conflict of interest with their obligation to act on behalf of a consumer”*[8]. The ACCC recommended that the ban on conflicted remuneration be extended to insurance brokers[9].

[5] NIBA, The economic value of insurance broking, prepared by Deloitte Access Economics, September 2020, p14 (***NIBA report***).
[6] This case study is taken from the NIBA report (p23), which has been adopted (and expanded) from the ACCC report (p20).
[7] ACCC report, p471.
[8] ACCC report, p480.
[9] ACCC report, recommendation 19.1.

QBE notes that certain disclosure requirements apply when insurance is sold through an intermediary. We recognise that reviews of the disclosure regime have indicated that the regime offers limited transparency and may not be adequate to manage conflicts of interest[10]. Since these findings, NIBA has updated its Insurance Brokers Code of Practice[11] (***Code***) in recognition of suggestions the Code could be improved to more adequately address conflicts of interest and commission remuneration structures. We note the Code now includes a ban on preferential remuneration and increased remuneration disclosure requirements.

QBE supports transparency and suggests that disclosure by insurance brokers be considered as part of the broader framework to manage conflicts of interest. We suggest the disclosure regime should be assessed, taking into account recent amendments to the Code (effective November 2022), to determine whether the regime is (or has the capacity to be) operating effectively.

Competitive considerations

Competition in the Australian general insurance market has been assessed in several inquiries[12] over recent years. Although some concerns have been expressed in relation to the level of competition for some segments of the market (typically where the nature of the risk is high), generally the findings are that the insurance industry is highly competitive.

Specifically in relation to insurance intermediaries, the ACCC estimates that approximately 35% of consumers buy home and contents insurance through an insurance intermediary[13]. This suggests that intermediaries play a significant role in distribution and driving competition, at least in the home and contents insurance market.

In 2017, a Senate Inquiry usefully characterised competition in the context of the general insurance industry as follows[14]:

> *Competition is the cornerstone of well-functioning markets, driving efficiency with regard to price, innovation, service and product quality, and providing better information that allows for more informed consumer choices. To that end, competitive markets deliver positive consumer outcomes and, by extension, increase the welfare and prosperity of all Australians.*
>
> *Healthy competition is integral to insurance affordability and accessibility. A lack of competition in insurance markets can result in negative consumer outcomes, such as premium increases, underinsurance, or coverage that is inappropriate to consumers' needs.*

We believe intermediated sales channels facilitate competition and innovation in the general insurance market. QBE believes it is important for the Review to also consider potential impacts on competition in the general insurance market, if the current exemption from the ban were to be removed. This should also include any potential flow on consequences to insurance affordability and availability.

Acquisition costs

Insurers incur acquisition costs associated with all forms of distribution, whether direct or intermediated distribution. Direct insurers may incur these costs in the form of staff training, marketing and advertising, call centres and IT systems for instance, while intermediated insurers generally incur distribution and sales costs in the form of commissions paid to distributors such as agents or brokers.

As the ACCC has noted[15]:

> *Commission costs for an insurance policy will depend on the way the policy was purchased. Where a policy is purchased directly from an insurer, there will be no commission costs (although the operating costs component may be higher as the insurer will spend more on things such as marketing and sales when selling directly). However, where the insurance is purchased through an insurer intermediary, such as a distributor, authorised representative, or another intermediary who sells insurance on behalf of an insurer, or an*

---

[10] FSRC, Final Report, Volume 1, February 2019, p174 and ACCC report, p480.

[11] NIBA, Insurance Broker Code of Practice, March 2022 (effective November 2022).

[12] For example, ACCC report, the Senate Economics References Committee, Australia's general insurance industry: sapping consumers of the will to compare (***Senate Inquiry***) (August 2017), the Productivity Commission's Final Inquiry Report into Competition in the Financial System (June 2018) and the Financial System Inquiry Final Report (December 2014).

[13] ACCC report, p17.

[14] Senate Inquiry, p21.

[15] ACCC report, p70.

insurance broker engaged by a consumer, there will usually be some commission included in the premium paid.

Case study – treatment of acquisition costs in the NSW Compulsory Third Party (CTP) Scheme

Insurers' customer acquisition strategies were considered in the context of recent major reforms to the NSW CTP Scheme. This provides a useful example in considering the nature of acquisition costs associated with insurance distribution.

Specifically, in the final report of the Independent Review of Insurer Profit within the NSW CTP Scheme, it was found[16]:

"Insurers have different customer acquisition strategies, with acquisition costs in recent premium filings varying between 3% and 13% of premiums. 'Direct' insurers sell policies directly to consumers and target acquisition expenditure at the level of the consumer. 'Indirect' insurers sell policies through brokers, and correspondingly target acquisition costs at brokers, rather than consumers.

The current Scheme imposes a limit on commissions of 5% of premium, which only affects indirect insurers. … as there is no corresponding limit on acquisition expenses for direct insurers, this ***limit places indirect insurers at a disadvantage and creates an un-level playing field between insurers in the market. The Review believes that distribution models should be treated equally****, and that the current limit on commissions damages competition." [Emphasis added].*

Although the cap on commissions remains a feature of the NSW CTP Scheme, the current requirements provide for maximum rates of assumptions to be used in the determination of premiums, including "acquisition and policy-handling expenses, including commission and other remuneration, are subject to a maximum rate of $43.60 per policy (on average across the policies underwritten by an insurer), indexed with movement in CPI"[17]. That is, the maximum rates apply to all acquisition costs, irrespective of whether these costs are associated with direct or indirect distribution.

It is critical that the regulatory regime does not inadvertently favour one distribution model over another. Any reform proposal that operates to provide an advantage to some insurers over others creates an un-level playing field and could have a detrimental effect on the competitiveness of the general insurance market. As ASIC has acknowledged specifically in the context of a potential ban on conflicted remuneration for general insurance products *"there is a risk that a ban could result in a drop in the level of sales of some products; and a reduction in competition, if insurers who are largely dependent on intermediaries exit the market"*[18].

Small business intermediaries

There are many insurance intermediaries operating in Australia, including small businesses. For instance, NIBA members include over 400 medium and small insurance broking firms operating in cities, towns and regions across Australia. We strongly suggest potential impacts for small business insurance intermediaries of any proposed remuneration reforms should be carefully considered by the Review given the potential implications for these businesses and competition.

These small businesses also provide a vital service to communities in times of natural catastrophes. Where insureds need support in managing their claims, intermediaries will often manage the process on their behalf.

Insurance availability and under-insurance

It is challenging to assess levels of underinsurance and non-insurance. The ACCC report indicates while its consumer research enables inferences to be made about the potential for underinsurance, it is not possible to estimate underinsurance across a general region with confidence. In respect of non-insurance, the ACCC utilised a number of data sources, noting limitations, to find that rates of home building non-insurance is around 20% in Northern Australia and around 11% across the rest of Australia[19].

NIBA has indicated that, on average, brokers estimated that 45% of their new clients were existing business that were underinsured or not insured, prior to engaging a broker[20]. NIBA indicates that brokers facilitate greater choice and competition in the insurance market and more appropriate purchasing of insurance[21] (i.e. reducing underinsurance), which protects consumers and promotes more efficient market outcomes.

As outlined above, potential regulatory reforms impacting remuneration for intermediaries may have broader impacts on the insurance market – both insurers and intermediaries may re-price, modify or withdraw their

---

[16] Report of the Independent Review of Insurer Profit within the NSW Compulsory Third Party Scheme, October 2015, p54.

[17] State Insurance Regulatory Authority (***SIRA***), Motor accident guidelines, version 8.2, Guideline 1.59(b).

[18] ASIC, Submission to the FSRC Round 6: Insurance, 25 October 2018, p15.

[19] ACCC report, p267.

[20] NIBA report, p26. Note, 36% of business was underinsured and 9% of existing business was not insured at all – estimate based on a survey of brokers about the new clients gained in 2019 and their level of insurance prior to engaging their broker.

[21] NIBA report, p14.

services, and this may particularly impact small businesses intermediaries. This in turn will have impacts on competition and the availability and affordability of insurance to consumers. QBE suggests these broader implications should also be considered in any reform proposals.

Conclusion

QBE appreciates the opportunity to respond to the Issues Paper consultation and would be pleased to discuss or provide any further information to support this submission.

Should you have any questions or require further clarification or information, please do not hesitate to contact Kate O'Loughlin, General Manager Government Relations & Industry Affairs (kate.oloughlin@qbe.com).

QBE