



23 December 2015

By email: lifeinsurance@treasury.gov.au

Manager, Financial Services Unit
Financial System Division
The Treasury

Dear Sir or Madam

Life Insurance Reform Legislation

The Consumer Action Law Centre (**Consumer Action**) welcomes the opportunity to comment on the exposure draft *Corporations Amendment (Life Insurance Remuneration Arrangements) Bill 2015 (the draft bill)*.

Briefly, this submission:

- urges the Government to hold firm on the model endorsed by the Assistant Treasurer on 6 November 2015. The life insurance industry must not be permitted to use this consultation process to further weaken reforms to how life insurance advisers are remunerated;
- recommends changes to the grandfathering arrangements to ensure that transactions entered after the commencement date are subject to commission and clawback requirements, whether or not the transaction is entered with an existing client or is related to insurance bought before the commencement date; and
- recommends that the 2018 review should have broad terms of reference, and allows Government to retain the option to require level commissions, or make any other change to remuneration that is called for at the time.

About Consumer Action

Consumer Action Law Centre is an independent, not-for profit consumer organisation based in Melbourne. We work to advance fairness in consumer markets, particularly for disadvantaged and vulnerable consumers, through financial counselling, legal advice and representation, and policy work and campaigns. Delivering assistance services to Victorian consumers, we have a national reach through our deep expertise in consumer law and policy and direct knowledge of the consumer experience of modern markets.

Broadly

Consumer Action has long had concerns that the high commissions paid to life insurance advisers lead to poor outcomes for consumers. This concern is based in many years of experience with commission-based sales practices in door-to-door sales, timeshare, 'add-on' financial products,

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vocational education and training and many other markets where commissions lead to aggressive, misleading and unconscionable sales practices. ASIC report 413 *Review of Retail Life Insurance Advice* confirmed that there are also widespread problems in the sale of life insurance advice that can be traced back to commissions.

The industry reform model, endorsed by the Assistant Treasurer on 6 November 2015, is an improvement on current arrangements, but we are yet convinced that capping commissions at 60 per cent of first year premiums and legislating clawback periods will stop the kind of mis-selling exposed in ASIC Report 413. As long as life insurance advisers are paid commissions to sell insurance, they will have an incentive to put their own interests ahead of their clients. Even the commissions available to people selling Consumer Credit Insurance, capped at 20 per cent, have not controlled widespread mis-selling in that industry.¹ Best interest duties, adviser education, codes of practice and ethical standards are a partial solution, but the only way the interests of advisers and their clients can be aligned is to eliminate all forms of conflicted remuneration.

John Trowbridge's *Review of Retail Life Insurance*², while not removing commissions, did set out a plan for advisers to move away from commissions over time.³ Since then, remuneration reform for life insurance advice has been weakened twice after concerted lobbying by the industry. It is important that the current consultation process is not allowed to be used by the life insurance industry to further weaken reforms to how life insurance advisers are remunerated.

We support the draft bill in its approach to extending the existing ban on conflicted remuneration to benefits paid in relation to life risk insurance. Adopting the broad definitions of 'benefits' and 'conflicted remuneration' in the Corporations Act is positive, so that benefits include commissions as well as volume bonuses. In our view, sales targets of any kind have a similar distorting effect and should be banned.

Grandfathering arrangements

The proposed grandfathering arrangements will allow advisers to continue to charge commissions above the caps set by ASIC when increasing premiums on products sold before the commencement date. The explanatory memorandum explains this in the following example:

Example 1.3: Arrangement entered into before commencement date, life product issued before commencement date.

Insurer B and a licensee have an arrangement in place before the commencement date under which Insurer B pays the licensee upfront and ongoing commissions on life products sold by the licensee. Under the arrangement, if the premium increases due to additional cover being taken up, an additional upfront commission will be paid to the licensee by Insurer B.

The licensee has a client, Client X, who has a life insurance policy with Insurer B that was sold by the licensee. The life insurance policy was issued before the commencement date.

¹ See for example Consumer Action *Junk Merchants: How Australians are being sold rubbish insurance and what we can do about it* (December 2015); ASIC report 256 (2011) *Consumer Credit Insurance: A review of sales practices by Authorised Deposit-Taking Institutions*; ASIC report 361 (2013) *Consumer Credit Insurance Policies: Consumers' claims experiences*.

² John Trowbridge, *Review of Retail Life Insurance Advice: Final Report*, 26 March 2015.

³ At page 7. Trowbridge's proposal retained an upfront payment but was consciously designed to prompt advisers to start introducing fees for service.

On 2 July 2016, Client X seeks additional cover under the life insurance policy that results in a premium increase. As the arrangement was entered into before the commencement date, and as the life product was issued before the commencement date, the amendments do not apply, and the benefits paid do not need to meet the criteria specified by ASIC.⁴

We oppose the 'grandfathering' of commissions in this scenario. When a consumer and an adviser agree to increase cover on an existing policy, they are striking a new bargain. If this bargain is struck after the commencement date for a new law, that new law should apply.

The licensee in example 1.3 has already been paid for their work under the old commission structure and would continue to collect any ongoing commissions agreed under the old structure. Applying the new law to transactions which happen in the future is entirely legitimate, regardless of whether those transactions are with existing clients or extensions of existing policies. Allowing advisers to keep the pre-commencement commissions on bargains struck after the commencement date creates a significant incentive for the adviser to push their client to extend cover under their existing policy in all circumstances, regardless of whether the client needs more cover or whether the existing policy is the best one for their needs. This unwelcome incentive becomes stronger every year of the transition period as the commission for selling a different product falls. This is exactly the kind of conflict that this reform is trying to eliminate.

We recommend that the draft bill and explanatory memorandum be amended to ensure transactions entered after the commencement date are subject to the new commission and clawback requirements, whether or not the transaction is entered with an existing client or is related to insurance bought before the commencement date.

2018 review

We welcome the decision to commission ASIC to conduct a review of the new life insurance arrangements in 2018, and the indication that the Government will mandate level commissions if adequate progress has not been made in aligning the interests of firms and consumers. However, the review should have broad terms of reference, and it is important that the 'pass mark' for industry is set high enough to ensure real progress is made.

The explanatory memorandum explains that the Government will mandate level commissions if there has not been 'significant improvement' towards 'aligning the interests of firms and consumers'.⁵ In our view, the purpose of the 2018 review should be to assess what has been done and what further improvements can be made. ASIC should conduct a wide ranging review, and Government should retain the option make any change to remuneration that is called for at the time. Progress towards removing conflicts of interest should not be enough to protect the life insurance industry from further intervention if significant conflicts still remain. The 2018 review should also assess industry progress on widening Approved Product Lists (**APLs**). If APLs are still too limited by the time of the review, Government should impose the Trowbridge report recommendation that every licensee include at least half of the authorised retail life insurance providers on its APL.

⁴ At paragraph 1.45.

⁵ At paragraph 2.35

Please contact David Leermakers on 03 9670 5088 or at david@consumeraction.org.au if you have any questions about this submission.

Yours sincerely

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