



25 November 2016

Committee Secretary  
Parliamentary Joint Committee on Corporations and Financial Services  
PO Box 6100  
Parliament House  
Canberra ACT 2600

**By email:** [corporations.joint@aph.gov.au](mailto:corporations.joint@aph.gov.au)

Dear Sir/Madam,

**Submission: Life insurance industry inquiry**

Thank you for the opportunity to provide comment to the Parliamentary Joint Committee on Corporations and Financial Services' Inquiry into the life insurance industry (the **Inquiry**).

This submission will focus on issues seen in Consumer Action's casework and policy work, including life insurance contract terms which could be 'unfair', an assessment industry self-regulation and problematic insurance products and sales practices, in particular funeral insurance and 'add-on' life insurance. Case studies in this submission have been de-identified.

Our comments are detailed below.

## 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.

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## Recommendations

This submission makes the following recommendations:

1. The unfair contract terms prohibition under the Australian Consumer Law (**ACL**)/*Australian Securities and Investments Commission Act 2001* (Cth) (**ASIC Act**) should apply to all insurance contracts, including life insurance.
2. The Life Insurance Code of Practice should be improved and registered with ASIC.
3. The life insurance and superannuation industries should work to ensure that people who make claims under group insurance policies super have stronger protections and rights, particularly in relation to claims timeframes, investigations and surveillance.
4. In relation to the critical issue of medical definitions in life insurance policies:
  - industry-wide standard medical definitions should be independently reviewed and regularly updated;
  - people who are buying or have life insurance should be able to easily access information about what medical definitions apply to their policies and why;
  - current medical definitions should ultimately apply to all life insurance policies, to address the serious problems seen in the CommInsure scandal; and
  - as an immediate step, the life insurance industry should be more transparent about what impact the application of updated medical definitions to insurance policies will have on premiums.
5. Life insurance products should not be sold as 'add-on' insurance.
6. Funeral insurance products should be improved so that, at a minimum:
  - funeral insurance is not sold to people under 50 years, at the absolute youngest;
  - premiums are fixed for the life of the policy, and stepped premiums are prohibited; and
  - premiums cease once the benefit amount is reached (or a very small % above that). Insurers have the benefit of holding the money paid in premiums, which should be sufficient for their profit.

Consumer Action also endorses the submission of Financial Rights Legal Centre to this inquiry in relation to:

- funding legal services to assist consumers with insurance problems;
- improved dispute resolution for consumers in disputes with insurers;
- improved disclosures in insurance policy renewal notices; and
- regulating insurers' use and collection of consumer data.

## Recent developments

There has been broad acknowledgement recently that more must be done to protect people when they buy or make a claim on life insurance.<sup>1</sup>

### ASIC

ASIC has reported systemic problems with the life insurance industry.

In particular, in 2014 ASIC reported that 37% of retail life insurance advice failed to comply with laws relating to appropriate advice and prioritising the needs of the client.<sup>2</sup> Following ASIC's report, the insurers commissioned the independent Trowbridge review, which recommended a package of changes to commissions, benefits and approved products lists, steps to improve consumer understanding, and a Code of Practice for insurers, licensees and advisers.<sup>3</sup>

More recently, ASIC has identified considerable variation in declined claims among insurers, with 90% of claims overall paid, but denial rates being as high as 37% for TPD, 31% for trauma and 29% for direct life insurance.<sup>4</sup>

We acknowledge ASIC's significant work in this area, including its reports on retail life insurance advice, 'add-on' insurance sold through car yards, and life insurance claims handling.<sup>5</sup> We support ASIC's continued work, in particular a review of direct life insurance, following the finding that it had higher claims denial rates than policies sold through advisers and group insurance policies. Our primary concern with direct life insurance is the adequacy of advertising, which plays on emotions and leads to purchases that may not be appropriate.

'Handling insurance claims' is currently exempt from the conduct provisions of Corporations laws.<sup>6</sup> We support ASIC's recommendation that this exemption be removed and that more significant penalties for misconduct in insurance claims handling be included in the review of ASIC's penalty powers.<sup>7</sup>

### Financial Systems Inquiry

The Financial System Inquiry (**FSI**) also made a number of recommendations that should improve consumer outcomes with respect to financial products, including life insurance.<sup>8</sup> The FSI found that the current disclosure arrangements are not sufficient to deliver fair treatment to consumers, noting that some consumers are sold financial products that are not suited to their needs and circumstances.

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<sup>1</sup> See for example The Hon Kelly O'Dwyer MP, *Media release: Release of ASIC report on claims handling in life insurance industry*, 12 October 2016; Adele Ferguson, 'Money for Nothing', *ABC News*, 7 March 2016.

<sup>2</sup> ASIC, *Report 413: Review of retail life insurance advice*, October 2014, *Report 471: The sale of life insurance through car dealers: Taking consumers for a ride*, February 2016 and

<sup>3</sup> John Trowbridge, *Review of Retail Life Insurance Advice: Final Report*, 26 March 2016.

<sup>4</sup> ASIC, *Report 498*, paras 2 and 29.

<sup>5</sup> ASIC, *Report 413; Report 471: The sale of life insurance through car dealers: Taking consumers for a ride*, February 2016; *Report 498: Life insurance claims: An industry review*, October 2016.

<sup>6</sup> *Corporations Regulations 2001* (Cth) reg 7.1.33.

<sup>7</sup> ASIC, *Report 498*, para 48.

<sup>8</sup> Financial System Inquiry, *Final Report*, November 2014, p xxv.

The FSI made recommendations to improve the design and distribution of financial products through strengthening product issuer and distributor accountability, and through implementing a new temporary product intervention power for ASIC. The Government has accepted these recommendations and promised to ‘accelerate’ their implementation.<sup>9</sup> Consumer Action strongly supports this work, and notes that the implementation of these reforms will need to be robust, so that effective obligations are not watered down during the legislative process.

### **Current and future reforms**

Consumer Action welcomes the government’s moves to cap commissions on retail life insurance advice and provide for clawback arrangements.<sup>10</sup> We are keen to see the impact of this reform. In our view, if there is no significant improvement in practices and consumer outcomes as a result of the commissions cap, a prohibition on conflicted remuneration in life insurance sales would be warranted.

There are also other areas which are ripe for reform. These include:

- extending the unfair contract terms regime to insurance contracts; and
- prohibiting the sale of ‘add-on’ life insurance.

### **Unfair contract terms**

An obvious gap in the legislative scheme for life insurance is the exemption of insurance contracts from the prohibition on unfair contract terms (UCTs) under the ASIC Act.<sup>11</sup>

It has always been our view that there is no sound reason to carve out the insurance industry from these otherwise economy-wide provisions. Indeed the Productivity Commission’s 2008 review of Australia’s consumer policy framework (which recommended that that law include a prohibition on unfair contract terms in standard form contracts) argued for a single, generic consumer law to apply across all sectors of the economy finding ‘little reason for any variation’ in its content.<sup>12</sup>

As well as this in-principle support that consumer policy should be generic across Australia, the following bodies and inquiries have specifically supported the extension of unfair contract terms protections to insurance contracts:

- Senate Economics Legislation Committee report into the *Trade Practices Amendment (Australian Consumer Law) Bill 2009* (2009);<sup>13</sup>

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<sup>9</sup> The Hon Scott Morrison MP and The Hon Kelly O’Dwyer MP, *Media release: Turnbull Government bolsters ASIC to protect Australian consumers*, 20 April 2016, <http://sjm.ministers.treasury.gov.au/media-release/042-2016/>.

<sup>10</sup> Under the *Corporations Amendment (Life Insurance Remuneration Arrangements) Bill 2016* (Cth).

<sup>11</sup> Section 15 of the Insurance Contracts Act provides that a contract to which the Act applies is not capable of being made the subject of relief, under any other Act, in the form of judicial review on the ground that the contract is ‘harsh, oppressive, unconscionable, unjust, unfair or inequitable’.

<sup>12</sup> Productivity Commission, *Review of Australia’s Consumer Policy Framework*, Inquiry Report No 45, 2008. See for example, Vol 2, pp 58-61 and Vol 2, p 327.

<sup>13</sup> At para 10.13.

- Natural Disaster Insurance Review inquiry into flood insurance and related matters (2011);<sup>14</sup> and
- House of Representatives Committee on Social Policy and Legal Affairs inquiry into the operation of the insurance industry during disaster events (2012).<sup>15</sup>

While some of the above inquiries focused on general insurance, there does not appear to be a valid reason for the exclusion to apply to life insurance either. We note that in the report of the Senate Economics Inquiry into the *Trade Practices Amendment (Australian Consumer Law) Bill 2009* (Cth), which regulated unfair terms in consumer contracts, Coalition Senators 'agreed that unfair terms in insurance contracts exist and the problem should be addressed in the public interest', though Coalition Senators were divided as to whether unfair terms should be regulated under generic consumer law provisions or within the *Insurance Contracts Act 1984* (Cth) (**Insurance Contracts Act**).<sup>16</sup>

Under the UCT regime, a term of the consumer contract will be void if it is found to be unfair. A term will be "unfair" if:

- (a) it would cause a significant imbalance in the parties' rights and obligations arising under the contract; and
- (b) it is not reasonably necessary in order to protect the legitimate interests of the party who would be advantaged by the term; and
- (c) the term would cause financial or other detriment (e.g. delay) to a consumer if it were to be applied or relied on.

Terms that define the main subject of the contract (that is, the goods or services that are acquired under the contract, or a term that is necessary for the supply of goods or services to occur) or terms that set the upfront price payable are excluded.

If the UCT regime applied to insurance, we would likely see fairer contracts being sold by insurers. This is likely to mean that hidden or unfair exclusions or conditions would be removed, and reduce the likelihood of dispute and consumer harm. In life insurance, there would be a stronger onus on insurers to ensure exclusions and medical definitions had a reasonable basis.

Insurers argue that existing requirements in insurance regulation are sufficient to protect consumers. For example, the Insurance Contracts Act prevents an insurer from relying on a contract term if to do so 'would be to fail to act with the utmost good faith'.<sup>17</sup> The key weakness

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<sup>14</sup> Natural Disaster Insurance Review, *Inquiry into flood insurance and related matters*, September 2011, Recommendation 37, [http://www.ndir.gov.au/content/report/downloads/NDIR\\_final.pdf](http://www.ndir.gov.au/content/report/downloads/NDIR_final.pdf).

<sup>15</sup> House of Representatives Standing Committee on Social Policy and Legal Affairs, *In the Wake of Disasters—Volume One: The operation of the insurance industry during disaster events*, February 2012, para 7.22, [http://www.aph.gov.au/Parliamentary\\_Business/Committees/House\\_of\\_Representatives\\_Committees?url=spla/insurance/report/index.htm](http://www.aph.gov.au/Parliamentary_Business/Committees/House_of_Representatives_Committees?url=spla/insurance/report/index.htm).

<sup>16</sup> Senate Economics Committee, *Inquiry into Trade Practices Amendment (Australian Consumer Law) Bill 2009*, 2010, [http://www.aph.gov.au/Parliamentary\\_Business/Committees/Senate\\_Committees?url=economics\\_ctte/completed\\_inquiries/2008-10/tpa\\_consumer\\_law\\_09/report/d01.htm](http://www.aph.gov.au/Parliamentary_Business/Committees/Senate_Committees?url=economics_ctte/completed_inquiries/2008-10/tpa_consumer_law_09/report/d01.htm).

<sup>17</sup> Insurance Contracts Act s 14.

of this provision is that it relies on consumers—the weaker party—to proactively challenge the decision of insurers using a poorly understood and cumbersome process. While there is no shortage of consumers who have been harmed by unfair terms in insurance contracts, analysis by National Legal Aid has found that s 14 is rarely used by either consumers or ASIC, suggesting this mechanism is either inaccessible, ineffective, or both.<sup>18</sup>

### Alex's story

Alex had Total and Permanent Disablement (TPD) and Salary Continuance insurance cover for two years through his superannuation fund. He stopped work due to mental illness, but was keen to return to work. He made a claim for salary continuance benefits.

Alex's policy had a clause that required him to terminate his employment for benefits to continue past 12 months. He did not want to resign because he wanted to return to work, but he was worried about losing his house in the meantime. Alex eventually lost his job.

In 2013, a Bill was drafted by the previous government to extend unfair terms protections to general insurance contracts,<sup>19</sup> but lapsed before the 2013 election. We encourage the Committee to re-examine that Bill, and consider the benefits of extending its application to life insurance. Now is a prescient time for this reform, with the Australian Consumer Law Review Interim Report seeking views on the extension of the UCT regime to insurance contracts.<sup>20</sup>

### Mental illness exclusions

An insurer cannot lawfully discriminate against people on the basis of disability (or another attribute) unless:

- the discrimination is reasonable on the basis of actual and statistical data or, if that data is not available, on the basis of any other relevant factors; or
- avoiding the discrimination would cause an unjustifiable hardship for the insurer.<sup>21</sup>

The Financial Ombudsman Service (**FOS**) takes the view that an insurer must have actuarial data to back up such discrimination. FOS reports that in general insurance disputes where actuarial data is not relied upon, insurers have paid each claim.<sup>22</sup>

Although insurers routinely discriminate by denying cover for people with mental illnesses, there is no transparency as to the basis for insurers denying cover. Consumer Action is not aware that any actuarial data exists.

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<sup>18</sup> National Legal Aid, *Submissions to Senate Economics Legislation Committee Inquiry into the Trade Practices Amendment (Australian Consumer Law) Bill*, 14 August 2009, p 4, <http://www.nationallegalaid.org/assets/NLA-Submissions/2009-Submissions/L-NLA-SELC-Inquiryin2theTradePractAmend-14-08-09scan.pdf>.

<sup>19</sup> *Insurance Contracts Amendment (Unfair Terms) Bill 2013* (Cth).

<sup>20</sup> Consumer Affairs Australia and New Zealand, *Australian Consumer Law Review: Interim Report*, October 2016, p 117.

<sup>21</sup> *Disability Discrimination Act 1991* (Cth) s 46(1).

<sup>22</sup> 'Ombudsman slams 'discriminatory' mental health exclusions', *insuranceNEWS*, 12 September 2016, <http://insurancenews.com.au/local/ombudsman-slams-discriminatory-mental-health-exclusions>.

The archaic treatment of mental illness under insurance policies extends beyond life insurance. For example, in *Ingram v QBE Insurance (Australia) Limited*,<sup>23</sup> a travel insurance policy included a blanket exclusion of claims caused directly or indirectly by mental illness. VCAT found that the insurer discriminated against Ms Ingram through this exclusion. The insurer did so without any statistical data and not discriminating would not have caused the insurer unjustifiable hardship.

Mental health exclusions in life insurance have not received the same attention, although there are parallels with general insurance contracts such as travel insurance and the disability component of Consumer Credit Insurance (CCI), which is general insurance. Broad mental health exclusions are common place in both general and life insurance policies.

### **Example mental health exclusion**

[N]o Benefit will be payable under this Policy if the event giving rise to the claim is caused directly or indirectly by...

- Any mental health disorder, including: anxiety disorders and depression; stress or adjustment disorders; eating disorders; emotional or behavioural disorders; drug or alcohol abuse; psychosomatic disorders, or any treatment complications.
- Fatigue: disorders related to fatigue, including chronic fatigue syndrome.
- Drug and alcohol related Sickness or Injury: taking intoxicating liquor (however, we will pay a claim if you are at or under the legal blood alcohol limit for driving); taking drugs (unless prescribed to you by a Medical Practitioner and taken in the correct dose).<sup>24</sup>

Mental health exclusions have had harsh and unfair impacts for Consumer Action's clients. Many people's claims have been denied on the basis of broad mental health exclusions. Others have their claims accepted, but only after significant and lengthy disputes. People navigate these processes while dealing with extraordinary personal, health and financial difficulties.

### **John's story**

In May 2015, John stopped working due to his mental illness. He saw his doctor a few days after he stopped work. In February 2016, John made a disability claim under his CCI policy. In March, the insurer declined the claim, saying that:

- John had not provided evidence that he was working 'immediately before' he became disabled; and

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<sup>23</sup> *Ingram v QBE Insurance (Australia) Limited (Human Rights)* [2015] VCAT 1936 (18 December 2015).

<sup>24</sup> InsuranceLine Income Protection Plus: Combined Product Disclosure Statement and Financial Services Guide, 26 August 2016, p 26, [https://www.insuranceline.com.au/~/\\_/media/PDS/income-protection-pds.ashx](https://www.insuranceline.com.au/~/_/media/PDS/income-protection-pds.ashx).

- his claim was caused by 'disturbance of the mind' due to alcohol—which was grounds to deny the claim.

John asked the insurer to review the decision because:

- he saw his doctor only a few days after he stopped work, so the insurer should not decline his claim on the basis that he was not employed 'immediately before' disablement; and
- there was no evidence that he was suffering from any disturbance of mind or faculty due to alcohol or drugs.

The insurer maintained that it denied the claim.

Consumer Action wrote to the insurer on John's behalf, requesting that the insurer review its decision. We enclosed a further report from John's doctor clarifying that his view was that John was unable to work from the date he left work.

In September 2016, the insurer finally accepted John's claim.

Consumer Action encourages the Committee to examine why, in the context of increasing awareness and understanding of mental illness throughout the community, insurers continue to deny liability on the basis of broad mental health exclusions in insurance policies.

#### Drug and alcohol exclusions

Alcohol is a contributing factor in a significant number of deaths in Australia each year. A joint health services report in Victoria in 2014 found that in 2010 4.7% of deaths in Australian men to alcohol and 3.0% of deaths in females were attributable to alcohol.<sup>25</sup>

#### **Burden of alcohol attributable diseases in Australia**

- There were 5,554 deaths attributable to alcohol in 2010, including 3,467 male deaths and 2,087 female deaths.
- In males, injuries were responsible for the highest proportion of alcohol-related deaths (36%), followed by cancers (25%) and digestive diseases (16%). For females the highest proportion of alcohol-attributable deaths was for cardiovascular diseases (34%) followed by cancers (31%) and injuries (12%).<sup>26</sup>

Despite the prevalence of alcohol-related deaths in Australia, there are again broad drug and alcohol exclusions in life insurance policies.

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<sup>25</sup> VicHealth, Turning Point and FARE, *Alcohol's burden of disease in Australia*, 31 July 2014, pp 59-60.

<sup>26</sup> VicHealth, Turning Point and FARE, *Alcohol's burden of disease in Australia*, 31 July 2014, p vii.

### Example: Drug and alcohol exclusion

*We will not pay a benefit or refund any premiums under your policy if the claim, directly or indirectly, is a result of... Your consumption of alcohol or drugs, other than those prescribed by a registered doctor and taken as directed.<sup>27</sup>*

Alcohol dependence is a mental illness and therefore a 'disability' under the law.<sup>28</sup> This means the same requirements sit on insurers as for other mental health exclusions if they discriminate on the basis of alcohol dependence.

Consumer Action has seen clients face significant hurdles in trying to claim on life insurance where the insurer determines that an alcohol exclusion applies.

### Bob's story

Bob's daughter Carol had complex mental health issues. She was alcohol dependent and had been for a number of years.

In mid-2015, Carol was hit by a car and killed. The Coroner's report did not draw conclusions about any direct or indirect link between Carol's consumption of drugs or alcohol and her death, and concluded that her death was accidental, but did note that alcohol was present in her blood.

Bob made a claim on Carol's life insurance policy. Carol's policy excluded a claim if the claim was 'a direct or indirect result of' alcohol or drugs. In mid-2016, the insurer denied the claim.

Bob is now caring for Carol's young children. His dispute with the insurer continues.

The broad reading of exclusions such as those in Rick's policy can mean significant uncertainty and protracted disputes for people who can withstand the claims process.

We encourage the committee to examine how broadly excluding drug and alcohol-related deaths is affecting the suitability of life insurance for many people in Australia.

### UK laws

As noted above, the *Insurance Contracts Amendment (Unfair Terms) Bill 2013* (Cth) before the previous Parliament would have extended the UCT regime to general insurance contracts. We would welcome similar laws as a step towards the application of a UCTs prohibition to all insurance contracts.

In the United Kingdom, the *Consumer Rights Act 2015* (UK) (**Consumer Rights Act**)<sup>29</sup> applies to general and life insurance contracts, however core terms such as exclusions are exempt

<sup>27</sup> AAMI Life Insurance Express: Combined Product Disclosure Statement and Policy Document, 30 March 2015, p 10, <https://www.aami.com.au/content/dam/suncorp/insurance/aami/documents/life-and-income/pds-life-insurance-express-30-03-15.pdf>.

<sup>28</sup> *Disability Discrimination Act 1992* (Cth), s 4.

<sup>29</sup> Part 2 covers unfair terms.

from the UCTs prohibition.<sup>30</sup> Importantly, this exemption only applies if the clause in question is ‘transparent’ and ‘prominent’, which are both defined.<sup>31</sup>

The Consumer Rights Act also includes a ‘grey list’ of terms that are presumed to be unfair, and which apply to insurance contracts. These include disproportionately high cancellation charges and terms which allow an insurer to determine characteristics of the subject matter of the contract and/or discretion as to the price after the consumer has been bound.<sup>32</sup>

UK insurance consumers therefore enjoy stronger protections than Australian consumers currently. An Australian insurer can include any term in a contract, provided it acts in accordance with the duty of utmost good faith. As noted above, this has not proven to be a robust consumer protection. However, a UK insurer is restricted from including particularly egregious terms, and must take steps to ensure that consumers know and understand the exemptions and other key clauses in their insurance documents before they sign.

Current consumer protections against UCTs in life insurance contracts are clearly inadequate. We encourage the Committee to consider applying a UCTs prohibition to insurance contracts.

### **Recommendation 1**

Insurance contracts should be brought under the unfair contract terms regime.

## **Industry Code of Practice**

The Financial Services Council (**FSC**) Life Insurance Code of Practice (the **Code**) has been slated as the industry’s response to significant problems experienced by people who buy life insurance or make a claim on their life insurance.

The independent Trowbridge report, commissioned by the Association of Financial Advisers and FSC, recommended a raft of changes including an industry Code ‘modelled on the general insurance Code of Practice, aimed at setting standards of best practice for life insurers, licensees and advisers for the delivery of effective life insurance outcomes for consumers’.<sup>33</sup>

In addition to this, the CommInsure scandal of March 2016 exposed deeply troubling practices by insurers when people make claims, and pointed to the devastating impact of out-of-date medical definitions in policies.<sup>34</sup>

In the context of increasingly loud calls for a Royal Commission into Australia’s banking system, the FSC stated in August 2016 that ‘Australia’s \$44 billion life insurance sector is part-way through its biggest reform agenda for decades’.<sup>35</sup> The Code, which was released on 11

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<sup>30</sup> Reference

<sup>31</sup> Consumer Rights Act s 64.

<sup>32</sup> Consumer Rights Act Sch 2 Pt 1.

<sup>33</sup> John Trowbridge, *Review of Retail Life Insurance Advice: Final Report*, 26 March 2015, p 60.

<sup>34</sup> Adele Ferguson, ‘Money for Nothing’, *ABC Four Corners*, 7 March 2016.

<sup>35</sup> Sally Loane, ‘Banks royal commission means death for life insurance reforms’, *Australian Financial Review*, 29 August 2016.

October 2016 and commences on 1 July 2017, appears to be the key element in the industry's self-regulation efforts. Consumer Action provided comment to the FSC during the development of the Code.<sup>36</sup>

As Consumer Action stated when the Code was released in October 2016,<sup>37</sup> it provides some significant improvements for people who make claims on their life insurance. In particular:

- it provides protections for people who are subjected to investigations and surveillance while their claims are being assessed, for example, by restricting where surveillance can take place—although there are examples of better provisions, for example the NSW Motor Accidents Authority Claims Handling Guidelines,<sup>38</sup> and
- it ensures that life insurance claims will be decided in a maximum of 12 months.

However, there are some significant weaknesses with the Code, including that:

- the Code is not enforceable by courts or tribunals, or registered with ASIC;
- the claims timeframes do not apply to people who have life insurance in their superannuation, which is the majority of life insurance,<sup>39</sup> and
- the three-yearly reviews by a 'relevant' medical specialist do not have to be undertaken independently of the insurers. The Code also only guarantees some updates to medical definitions for 'on sale' policies only, excluding the many people whose policies are no longer 'on sale'.

We note that the Minister for Revenue and Financial Services stated at the time of the Code's release:

The Government encourages the FSC and life insurance industry to continue to work on improving consumer outcomes in this vital sector of the financial system. Importantly, the Government expects that the FSC and industry will continue to work towards expanding the coverage and scope of the Code to more fully cover group insurance arrangements within superannuation, and will take the necessary steps to ensure that the Code is enforceable across the whole industry, by gaining ASIC approval of the Code.<sup>40</sup>

Consumer Action echoes the Minister's expectations.

The Code in its current form will not make significant headway towards addressing the Commlnsure scandal, nor the problems demonstrated in the ASIC and Trowbridge reports.

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<sup>36</sup> See Financial Rights Legal Centre and Consumer Action, *Draft Life Insurance Code of Practice*, January 2016, <http://consumeraction.org.au/8571-2/> and *Draft Life Insurance Code of Practice—Second Public Consultation*, September 2016, <http://consumeraction.org.au/draft-life-insurance-code-practice-second-public-consultation/>.

<sup>37</sup> Consumer Action and Financial Rights Legal Centre, *Media release: Life insurance code a modest first step, needs more work: Consumer Groups*, 11 October 2016, <http://consumeraction.org.au/life-insurance-code-modest-first-step-needs-work-consumer-groups/>.

<sup>38</sup> See <http://www.sira.nsw.gov.au/resources-library/motor-accident-resources/publications/professionals/guides-for/claims-handling-guidelines>.

<sup>39</sup> Life insurance held in superannuation funds accounts for 67% of sums insured: Rice Warner, *Insurance Administration Expenses*, August 2014.

<sup>40</sup> The Hon Kelly O'Dwyer, *Media release: Government welcomes release of Life Insurance Code of Practice*, 11 October 2016.

However, we are aware that the industry is making progress to address the weaknesses in the Code. This work includes:

- the establishment of the joint Insurance in Superannuation Industry Working Group, to develop a code of practice for superannuation fund trustees and insurers before the end of 2017;<sup>41</sup> and
- the FSC's development of standard minimum medical definitions for certain cancer, severe heart attack and stroke. These definitions are only an initial step in our view (see further below).

With the Code slated for review and improvement, there is still significant work to be done by the life insurance industry to ensure that everyone who buys or has life insurance has appropriate protections.

### **Recommendation 2**

The Life Insurance Code of Practice should be improved and registered with ASIC.

### **Recommendation 3**

The life insurance and superannuation industries should work together to ensure that people who make claims under group insurance policies super have stronger protections and rights, particularly in relation to claims timeframes, investigations and surveillance.

### **Medical definitions**

As the Commlnsure scandal showed, people's claims have been denied due to out-of-date medical definitions in their policies. Insurers continue to collect premiums every year for what may be increasingly unsuitable products. In our view this is a significant factor in the lack of consumer trust in insurers.

The FSC publicly stated in August 2016 that the Code would include standard minimum medical definitions, however this is currently not the case.<sup>42</sup> As noted above, the FSC is now developing three standard minimum medical definitions for cancer excluding early stage cancers, severe heart attack measured by specific tests, and stroke resulting in permanent impairment.

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<sup>41</sup> Association of Superannuation Funds of Australia and others, *Joint Media Release: Insurance in Superannuation Industry Working Group*, 2 November 2016.

<sup>42</sup> Sally Loane, 'Banks royal commission means death for life insurance reforms', *Australian Financial Review*,

Consumer Action has provided comment to the FSC on these definitions.<sup>43</sup> In summary, we have ongoing concerns with medical definitions in policies and the lack of independent review or guaranteed updates to these definitions. Key issues include:

- The life insurance Code requires medical definitions to be reviewed by ‘relevant’ experts, but these experts do not have to be independent of the insurers. This fundamentally undermines the appearance of impartiality and raises questions as to the validity of any review into medical definitions, in the eyes of consumers. We are strongly of the view that these reviews must be conducted independently, with open public consultation, if they are to hold any legitimacy or validity in the eyes of the community.
- There are necessarily technical terms and abbreviations in the definitions. Insurers should provide guidance on these, to make them more accessible for consumers, who are entitled to know what their policies cover.
- The FSC previously mentioned that there would also be a definition of by-pass. We believe that it is worth examining the possibility of including this definition.

Premium costs and coverage are a very contentious consumer issue when examining medical definitions. Where a change in definitions will potentially lead to more and/or higher value claims, then premiums are bound to change either at an individual policy level or for all policies.

We expect more transparency from insurers on the impact that updated definitions will have on premiums.<sup>44</sup> Improved transparency of coverage and costs should be a first step towards a longer-term goal of up-to-date medical definitions applying to all life insurance policies.

#### **Recommendation 4**

In relation to the critical issue of medical definitions in life insurance policies:

- industry-wide standard medical definitions should be independently reviewed, including with public consultation, and regularly updated,
- people who are buying or have life insurance should have easy access to information about what medical definitions apply to their policies and why,
- up-to-date medical definitions should ultimately apply to all life insurance policies, to address the serious problems seen in the CommInsure scandal, and
- as an immediate step, the life insurance industry should be transparent about what impact the application of updated medical definitions to insurance policies will have

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<sup>43</sup> Financial Rights Legal Centre and Consumer Action, *Submission: Financial Services Council—Draft Minimum Standard Medical Definitions*, November 2016, <http://consumeraction.org.au/financial-services-council-draft-minimum-standard-medical-definitions/>

<sup>44</sup> See Consumer Action and Financial Rights Legal Centre, *Submission: Draft Life Insurance Code of Practice—Second Public Consultation*, September 2016, pp 8-9, <http://consumeraction.org.au/draft-life-insurance-code-practice-second-public-consultation/>.

## Add-on insurance

There is broad acknowledgement of the problems with 'add-on' insurance, which is chiefly sold when people buy a financed motor vehicle.<sup>45</sup> Life insurance is sold as a component of add-on Consumer Credit Insurance (**CCI**), also known as Loan Protection Insurance, Mortgage Protection Insurance, Credit Card Insurance or Personal Loan Insurance. CCI insurance insures a person's ability to pay the loan. A 20% commission cap applies to personal-use CCI.<sup>46</sup> While CCI is predominantly a general insurance product,<sup>47</sup> there are also life components. Walkaway insurance, which pays out the loan, for example, in the event of accidental death, and 'trauma' insurance (for major illness) are other life insurance products sold as add-ons.

In February 2016, ASIC reported that there was a 'market failure and a lack of demand-driven competition' in the sale of life insurance in car yards.<sup>48</sup> The report found:

- Excessive prices relative to other life insurance products:
  - Personal-use car yard life insurance costs on average 50% more than life insurance sold through authorised deposit-taking institutions, with one insurer charging four times more,
  - business-use insurance, including that sold to small businesses (which is not subject to the 20% commission cap) were charged on average 40% more for the same products, and
  - for a low-risk consumer, insurers charge up to 10 times more for personal life insurance and 18 times more for business-use life insurance than under a term life insurance policy (the latter provides more cover).<sup>49</sup>
- Sales to people who did not want or need life insurance: Around 11% of car yard life insurance was sold to people aged 21 and under, whose would not need life insurance if they did not have dependants. 10% of all customers cancelled their policy in the cooling off period.<sup>50</sup>
- Extremely low claims ratios: Just 6.6c of every dollar paid in premiums was paid out in claims.<sup>51</sup>
- Single upfront premiums, which incur large interest charges: For example, an interest rate of 9% on a four-year loan of \$20,000 increases the cost of the insurance by 19.4%.<sup>52</sup>

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<sup>45</sup> See ASIC, *Report 470: Buying add-on insurance in car yards: Why it can be hard to say no*, 26 February 2016; ASIC, *Report 471: The sale of life insurance through car dealers: Taking consumers for a ride*, 29 February 2016; Consumer Action, *Junk Merchants: how Australian are being sold rubbish insurance and what we can do about it*, December 2015; Gilbert+Tobin (on behalf of Aioi Nissay Dowa Insurance Company Australia Pty Ltd and others), *Motor vehicle dealership add-on insurance reform: Application for authorisation*, 12 September 2016.

<sup>46</sup> National Credit Code s 145.

<sup>47</sup> Disablement cover under CCI is typically a general insurance component.

<sup>48</sup> ASIC, Report 471, para 4.

<sup>49</sup> ASIC, Report 471, p 7.

<sup>50</sup> ASIC Report, p 8.

<sup>51</sup> ASIC Report, p 8.

<sup>52</sup> ASIC, Report 471, p 8.

### **Jane's story**

Jane had a loan with finance company. She refinanced a number of times over 2012 to 2014. Each time, CCI was added with life, unemployment and disability components. Jane ultimately spent approximately \$6,000 in premiums over this time (not including interest) to insure a relatively small loan (ranging from \$3,600 to \$25,000).

Jane had diabetes, so the disability component was likely to be of limited value to her because of a pre-existing condition exclusion. She had no dependents, so life insurance was of little benefit. She also had life insurance and an account balance through her superannuation fund, which far exceeded her liability under the loan.

Jane remembers the finance company mentioning the insurance once, but does not remember them explaining what it was for or that it was optional. She did not realise that interest would apply to the premiums.

Jane said that, had she been given the choice, she would not have bought life insurance. She ultimately received a refund.

There have been steps to address this consumer detriment. Consumer Action assists people to claim refunds on 'junk insurance'.<sup>53</sup> Our [DemandARefund.com](http://DemandARefund.com) website enables people to write letters to insurers to demand refunds. This has so far seen 240 letters written claiming more than \$450,000 in refunds, with many receiving refunds. The insurance industry has applied to the ACCC to authorise a 20% cap on all commissions paid by insurers on insurance bought through car dealerships, to address the 'reverse competition' in the market.<sup>54</sup>

However, it is clear that the business model is broken. Particularly considering that many people hold life insurance in their superannuation, there is no demand or need for life insurance to be sold as an add-on.

### **Recommendation 5**

Life insurance should not be sold as 'add-on' insurance.

<sup>53</sup> See [DemandARefund.com](http://DemandARefund.com).

<sup>54</sup> Aioi Nissay Dowa Insurance Company Australia Pty Ltd & Ors applications for ACCC authorisation A91556-A91557, 13 September 2016. The decision in this application is due in February 2017. See Adele Ferguson, 'Car dealers claim add-on insurance limits could force them to close', *Australian Financial Review*, 21 November 2016, p 40.

## Funeral insurance

Consumer Action continues to see ongoing consumer detriment caused by funeral insurance being sold at high cost to people, including young children, who are highly unlikely to benefit from it. This has included large numbers of Indigenous people who have been targeted.<sup>55</sup> Many of our clients have paid more than the benefit sum under their insurance and many have also had to cancel their insurance because they could no longer afford the premiums.

A 2015 ASIC report in found that these policies had an 80% cancellation rate in 2014.<sup>56</sup> In addition, stepped premiums mean that premiums rise steeply for people after the age of 50, making them unaffordable for many people. ASIC also noted that some people have paid more in premiums than they were entitled to claim under the policy.<sup>57</sup>

Consumer Action was pleased to see the recent appeal decision of the Federal Court of Australia confirming the decision to exclude funeral insurance premiums from the Centrepay system, under which premiums are deducted directly from Centrelink payments.<sup>58</sup> The availability of Centrepay to make payments towards funeral insurance gave the product a sense of 'government approval', and meant that low income earners paid their limited income to pay for this form of expensive insurance, ahead of other essentials such as housing, energy or food costs. The removal of funeral insurance from Centrepay may go some way to improving the way these high-cost, low-value products are sold.

However, significant changes must be made to address the consumer harm caused by funeral insurance. It will be important for any reform to apply not only to products that provide a lump sum payment on the death of the insured (life insurance), but to products that provider for the cost of funeral expenses or burial only. These latter products enjoy exemptions from the *Life Insurance Act 1995* (Cth) and financial services licensing requirements.<sup>59</sup>

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<sup>55</sup> See for example 'Babies among thousands of Aboriginal children signed up to 'shocking' funeral insurance schemes', ABC News, 21 November 2015, <http://www.abc.net.au/news/2015-11-21/aboriginal-babies-being-signed-up-to-shocking-insurance-schemes/6958342>.

<sup>56</sup> ASIC, *Report 454: Funeral insurance: A snapshot*, October 2015, para 38.

<sup>57</sup> ASIC, *Report 454*, p 6.

<sup>58</sup> *Chief Executive Centrelink v The Aboriginal Community Benefit Fund Pty Ltd* [2016] FCAFC 153.

<sup>59</sup> See, eg, s761A and 765A(1)(w) of the *Corporations Act 2001*, s5(2)(a) and 12BAA(8)(o) of the *Australian Securities and Investments Commission Act 200* and s11(3)(e)(i) of the *Life Insurance Act 1995*.

## **Recommendation 6**

Funeral insurance products should be improved so that, at a minimum:

- funeral insurance is not sold to people under 50 years of age, at the absolute youngest,
- premiums should be fixed for the life of the policy, and stepped premiums should be prohibited, and
- premiums should cease once the benefit amount is reached (or a very small % above that). Insurers have the benefit of holding the money paid in premiums, which should be sufficient for their profit.

Please contact Susan Quinn on 03 9670 5088 or at [susan@consumeraction.org.au](mailto:susan@consumeraction.org.au) if you have any questions about this submission.

Yours sincerely,

**CONSUMER ACTION LAW CENTRE**



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