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Royal Commission into National Natural Disaster Arrangements (**Commission**)
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RESPONSE TO NOTICE TO GIVE INFORMATION NTG-HB1-008

About Consumer Action Law Centre

- Consumer Action is an independent, not-for profit consumer organisation with deep expertise in consumer laws and policy, and direct knowledge of people's experience of modern markets. We work for a just marketplace, where people have power and business plays fair. We make life easier for people experiencing vulnerability and disadvantage in Australia, through financial counselling, legal advice, legal representation, policy work and campaigns. Based in Melbourne, our direct services assist Victorians and our advocacy supports a just marketplace for all Australians.
- Consumer Action has provided advice and/or legal representation on insurance issues in 167 matters in the current financial year. Our work includes assisting people who have been denied insurance cover, who have bought unsuitable insurance or who have claims disputes with insurers. Through a model of secondary consultations, we also assist financial counsellors, community lawyers and other community workers to assist their clients with insurance matters. We most commonly assist people with disputes about car insurance, add-on insurance, home insurance and life insurance.
- Since 2016, Consumer Action's free tool DemandaRefund.com has helped people to demand over $23 million in refunds on junk add-on insurances sold by insurers, banks and car dealers.
- In addition to our direct services, Consumer Action is a member of Disaster Legal Help Victoria (**DLHV**),[1] a joint initiative of Victoria Legal Aid, the Federation of Community Legal Centres, Justice Connect, the Law Institute of Victoria, and the Victorian Bar that provides free legal advice and assistance and referrals to Victorians affected by a disaster. DLHV was originally formed to provide free legal support for those affected by the February 2009 Victorian bushfires.

Introductory comments

- In response to the specific questions asked in Notice to Give Information NTG-HB1-008 (**Notice**), our response focuses on insurance and natural disasters. Consistent with the Notice, this response uses the term 'natural disaster'.[2] We acknowledge, however, that the extreme weather and other impacts of climate change are not only caused by natural events – they are impacted by human action (and inaction).
- Australia is experiencing one of its worst disasters on record. People have lost their loved ones. Hundreds of families have lost their homes. Thousands more have seen their businesses, jobs and workplaces affected, first from Black Summer, now compounded by COVID-19. People take out insurance for peace of mind but, during this time of great difficulty, people cannot be certain that their home insurance will cover their losses and help get them back on their feet. Others could not afford insurance in the first place.
- This response makes recommendations to prevent the consumer harm we see from insurance in the context of extreme weather and climate change. The following key reforms will improve insurance outcomes ahead of the next fire season:

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[1] Justice Connect Pro Bono Referrals, *Bushfire-related insurance matters referred for pro bono assistance*, 6 April 2020.
[2] According to the Notice, a 'natural disaster' is a naturally occurring rapid onset event that causes a serious disruption to a community or region, such as flood, bushfire, earthquake, storm, cyclone, storm surge, tornado, landslide or tsunami.

- Establish an independent inquiry into the affordability of insurance to examine policy solutions at the complex intersection of insurance, financial hardship, and worsening climate change;
- Make insurance policies comparable by:
  - standardising key definitions in insurance contracts, including the definition of 'fire';
  - modernising 'standard cover' so that people can compare and choose suitable insurance policies;
- Pass the outstanding Financial Services Royal Commission[3] reforms, especially those impacting insurance claims handling, as a matter of urgency to ensure fair treatment of people by insurance companies;
- Establish a permanent insurance price monitor; and
- Increase funding to community legal centres that advise and represent people in their disputes against insurance companies to reduce the power imbalance and ensure fair outcomes for people.

- We also comment on non-insurance issues relevant to the Commission's Terms of Reference, including financial hardship responses by banks.
- A full list of recommendations is available at Appendix A on page 20.

1. In the context of the 2019-20 bushfires specifically, describe any issues which have arisen regarding: a. handling of claims (including timeframes for assessment); b. denial of cover (e.g. unexpected application of exclusions); c. underinsurance

- For the 2019-20 bushfires, one of the ways that DLHV provided pro bono legal assistance was by coordinating lawyers to visit the affected community to meet with people needing legal information and assistance at recovery centres. Victorians can also call DLHV or use webchat for information about their legal issues and options for ongoing assistance.[4] Consumer Action is available to receive referrals from DLHV on credit, debt, insurance and consumer law matters for Victorian residents.
- To date, Consumer Action has received only a small number of insurance enquiries relating to the 2019-20 bushfires. In our experience, insurance disputes, particularly in relation to claims handling or claims denial, tend to arise some months following the catastrophe. We suspect that COVID-19 may also be impacting referrals at present.
- We have received reports from community organisations that are operating in regional areas of significant delays in insurers undertaking assessments or arranging quotes for damage caused to properties in remote parts of Victoria.
- This leaves some people in extremely difficult circumstances, with their living situation and future in limbo. Financial counsellors have also reported concerns about people living in substandard accommodation, such as caravans, waiting for works to be undertaken, as well as people sleeping rough on their properties. The risk this poses only increases as winter approaches and with the COVID-19 pandemic.
- Service providers in remote areas have said that people had reported feeling forgotten before COVID-19, and that this has unsurprisingly only worsened since.
- Generally, the main issues we have seen in our DLHV legal casework during this and previous catastrophes in relation to home building and contents insurance are clients:
  - discovering when they make a claim that they are underinsured, that is, their sum insured is not adequate,
  - delays with the progress or claims or works; and

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[3] Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry (**FSRC** or **Financial Services Royal Commission**), *Final Report*, 1 February 2019: https://financialservices.royalcommission.gov.au/Pages/reports.aspx.
[4] For more information, see https://www.disasterlegalhelp.org.au/.

    - feeling pressured into accepting cash settlements which may not be adequate to repair or rebuild their homes.

Information from Victoria Legal Aid

- On 21 April 2020, Victoria Legal Aid confirmed to us that, as at 17 April 2020, DLHV had received the following insurance matters:
    - 14 calls to Victoria Legal Aid's Legal Help phone line – this includes inbound calls and outbound calls made by Legal Help resulting from referrals from recovery centres; and
    - nine legal advice records from lawyers attending at recovery centres.
- At 14 of 73 legal matters recorded from 108 answered calls, insurance matters were the most common legal matter recorded in Victoria Legal Aid's DLHV call data to date.

Information from Justice Connect pro bono referrals

- On 7 April 2020, Justice Connect pro bono referrals provided to us an overview of the insurance matters that it has referred to law firms for pro bono legal assistance in response to the 2019-2020 bushfires in New South Wales and Victoria.
- Below is a breakdown of matters by state and client type:
    - NSW: Total: 8; Individuals: 5; Small businesses/farms: 3
    - Victoria: Total: 4; Individuals: 4; Small businesses/farms: 0
- The following are outlines of a small sample of matters for clients assisted through Justice Connect:[5]
    - Individual, NSW: A couple whose family farm was destroyed sought advice about a dispute with their insurance company. Contrary to the clients' understanding of their insurance policy, the insurance company had claimed that only a couple of pieces of farm equipment were insured. The insurance company claimed that they had communicated the limited coverage of the policy to the client during a telephone conversation in 2016 for which they had no written record. After some negotiations, the insurance company agreed to backdate the insurance coverage to include sheds and fences from 2016. However, the insurance company required the clients to pay additional premiums for this to occur. Justice Connect referred this client to a member firm to assist with negotiations with the insurance company.
    - Small Business/Farm, NSW: A farmer's seafood farm was closed by the Environmental Protection Agency due to water runoff from firefighting efforts on an adjoining property. The farm's insurance policy only covered loss of equipment, not loss of stock. The client is obtaining advice from one of Justice Connect' member firms about the terms of their insurance policy, whether their loss would be covered by the insurance of the neighbouring property and whether they can access any Government grants. The farmer had found it difficult to find an insurance provider that was willing to cover stock that is so variable in value (that is, the farm could not predict accurately how much seafood it would produce with each crop).
    - Individual, Victoria: The client acted as a farm property manager in exchange for living in his mobile home on the property, at no cost. Both the client and landowner lost their homes in the fires. The landowner had indicated he would share the insurance payout and included details of the client's lost belongings in making a claim. The landowner later reneged on his promise to share the payout. Justice Connect referred this client for pro bono advice about the client's rights to make a claim against the landowner and their insurance payout. Justice Connect has assisted several clients who have suffered losses due to the bushfires but who are reliant on insurance policy holders to make claims on their behalf (and to then share insurance payouts with them in good faith). It is likely that there are many other people in this position.

[5] Justice Connect has obtained consent from the clients to provide these anonymised case stories for the purpose of reporting to the Royal Commission into Natural Disaster Arrangements.

- These statistics are not comprehensive of all legal assistance provided in relation to insurance matters – for example, the Insurance Law Service is another community legal service that provides advice nationally.[6]

2. Having regard to current trends regarding climate, and the rate of occurrence of natural disasters within Australia, can the Consumer Action Law Centre identify any systemic issues which are emerging regarding:

a. availability of cover

- We are concerned about the potential for premium rises following Black Summer, leading to affordability problems and people dropping out of insurance coverage. This issue should be monitored by the Australian Competition and Consumer Commission (**ACCC**) or a federal price monitor (see our comments at page 17 in response to Question 3 below).
- Embargoes may be introduced by individual insurers according to their own underwriting rules, typically preventing insurance being purchased when an event is known to be extremely likely or already impacting an area. One community lawyer reported to us concerns about the transparency of embargoes in regional Victoria, noting that it was unclear why the embargo was introduced, how long it would last, and the postcodes embargoed. Further, where the embargo applies to a particular postcode, this can cover large areas of land in regional Victoria, which may face different fire risk.

b. affordability of premiums, including for community infrastructure

Affordability for personal home and contents insurance

- As the risk of natural disasters or significant weather events increases, insurance premiums will almost certainly increase without intervention. The cost of insurance is always going to reflect the risk taken on and the likelihood of a claim being made, among other factors.
- The impact a greater risk of natural disasters or adverse weather events has on insurance premiums is demonstrated by the information collated by the ACCC in its inquiry into the supply of building home and contents insurance in northern Australia (**ACCC Inquiry**).[7]
- The ACCC Inquiry's second interim report detailed the significantly higher prices paid for home and contents insurance in northern Australia compared to the rest of the country.
- As part of the Inquiry, the ACCC sought to break down the components of pricing that make up a premium. It reported that 'peril components' – being the amount of an insurance premium determined by risk to perils (in that case, predominantly cyclones and floods), made up the largest proportion of premiums in northern Australia.[8]
- Areas more likely to be impacted by natural disasters are also more likely to have higher claim rates, which also tends to increase insurance premiums.
- An issue also identified from the data obtained by the ACCC Inquiry was that premium prices had increased far more in northern Australia than the rest of the country over the last decade. One factor that had caused significant price jumps over this period was that insurers had changed their methodology for determining risk. Insurers have moved toward more detailed forms of assessing risk over time, such as basing risk on a specific address, rather than postcode.
- This allows for a more accurate and realistic assessment of risk, but has seen insurance premiums rise in more cyclone and flood prone areas, and for specific properties at greater risk.[9] While this price might more accurately reflect the risk, it means that costs are likely to directly increase for those who need insurance the most, moving insurance away from its historic role of sharing risk at a community level. Specific risk factors for properties in acutely disaster-prone areas are having a greater impact than ever on the individual pricing of insurance policies.

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[6] https://insurancelaw.org.au/.
[7] https://www.accc.gov.au/focus-areas/inquiries-ongoing/northern-australia-insurance-inquiry.
[8] ACCC Inquiry, *Second Interim Report*, December 2019, p156-158; 205-209.
[9] ACCC Inquiry, *Second Interim Report*, December 2019, p202-204.

- Of concern is that, in the absence of government intervention, people experiencing affordability issues or financial difficulty are less able to fund mitigation works at the property level.[10]

- We have significant concerns about how this will play out as the impact of climate change worsens, particularly for regional parts of Australia where climate change means bushfires will be more frequent, and more severe. It was recognised in the Letters Patent of this Royal Commission that this is the reality Australia is facing. For Australians who live in areas increasingly at risk from bushfires, premiums are going to continually (and sometimes rapidly) increase.

- If homeowners cannot afford to rebuild due to the of cost premiums or the impacts of underinsurance, then they will be forced to leave their community.

- The precise policy solutions for this complex intersection of financial hardship, insurance, and climate change necessitate a separate inquiry into insurance affordability. The ACCC Inquiry and the NSW Emergency Services Levy Insurance Monitor (**NSW ESLIM**) have undertaken useful work on affordability of insurance in Northern Australia and NSW, but to date this is piecemeal and does not examine the situation in Victoria and other states. Unfortunately, NSW ESLIM is due to be disbanded on 1 July 2020.

- These complex problems cannot be understood and resolved quickly, and not within the timeframes for this Royal Commission, particularly in light of the disruption caused by COVID-19. We therefore recommend an independent review of insurance affordability in Australia, having regard to the rising levels of financial difficulty and worsening impacts of climate change.

- Further, given the complexity of these issues, there is a need for Government, the insurance industry, and consumer groups to work together on an industry-wide response to the impact of climate change on the provision of insurance.

Responses to financial hardship

- Added to this complexity is the impact of financial difficulty generally, which can mean people struggle to pay insurance premiums. The financial hardship protections in the insurance industry are very limited by comparison to banking, energy or telecommunications sectors. The General Insurance Code of Practice includes hardship protections when people cannot afford to pay their excess when making a claim, but offer no protections or consistent options for consumers when ill-health or unemployment mean they cannot afford their premiums.

- Where premiums go unpaid, the insurance policy is generally cancelled by the insurer for non-payment of premiums after 30 or 60 days, depending on the policy, and after the insurer takes certain steps.

- The general insurance industry's current response to COVID19 provides an example of how hardship assistance volunteered by industry, even during a recognised catastrophe, tends to offer limited assistance to consumers. Insurers have only committed to very limited, and inconsistent, support measures for consumers during COVID19 despite widespread economic hardship.

- In our discussions with the Insurance Council of Australia and the larger general insurers, there has been a reluctance to commit to consistent, industry-wide hardship measures, such as proactive provision of temporary deferrals of premiums during COVID19 for consumer insurances. Some insurers have suggested options available to consumers may be to temporarily or permanently reduce their coverage, or consider cheaper plans. This is not hardship assistance – it is just a reduction in cost commensurate to the reduced risk taken on by the insurer.

- Generally, the only public statements from insurers directed to consumers in hardship encourage them to get in touch to discuss options, on their website. While some insurers may be willing to provide useful assistance, we fear the absence of any public commitment means far more people are likely to either accept that they must find a way to pay their insurance bills on time, or may consider letting insurance lapse. There appears to be limited consideration that COVID19 may have reduced risks for insurers (e.g. vehicles not being driven; people being at home reducing risk of break-in) and sharing these benefits with consumers.

[10] ACCC Inquiry, *Second Interim Report*, December 2019, p17.

- This is not dissimilar to the responses we see from insurers following natural disasters. At a time when consumers are trying to pick up the pieces of their lives and survive on limited resources, genuine financial relief can make a huge difference. Requiring finance industry members, like general insurers, to make basic but valuable and practical short-term financial relief available following natural disasters would go a long way to help customers make informed decisions and get back on their feet. Uniformly imposed forms of assistance would also be far simpler to communicate to customers.
- We expect this to be a worsening problem in light of COVID19 and the mass unemployment currently being experienced, particularly when the Federal Government's interim measures expire after six months, just in time for the next fire season.
- We comment on non-insurance hardship issue relevant to the Terms of Reference below.

- **Recommendation 1**: An independent expert panel review insurance affordability in Australia, having regard to the rising levels of financial difficulty and the worsening impacts of climate change.
- **Recommendation 2**: Federal and state governments, the insurance industry, and consumer groups work together on an industry-wide response to the impact of climate change on the provision of insurance.
- **Recommendation 3**: Improve hardship protections in the insurance industry.

c. the scope / understanding on the part of insureds of relevant exclusions

- The core problems which persist for consumers include:
  - Comprehension—the complexity of insurance policies means that most people cannot comprehend their policy in full,
  - Comparison—differences in terms, conditions and definitions make it difficult to compare policies, even where a person knows what features they want, and
  - Suitability—the comprehension and comparison problems mean that people end up with unsuitable insurance.
- Please refer to our comments at (h) and (i) below on these issues.

d. underinsurance

- Recent trends suggest that underinsurance will become an increasingly significant and widespread issue in areas where climate change is making the incidence of significant weather events and natural disasters more likely.
- Consumer Action considers underinsurance and non-insurance for core insurance products as a significant concern in natural disaster-prone areas. We consider core general insurance products to be home and contents insurance, and basic comprehensive car insurance products.
- A person is underinsured when their home and contents insurance benefits are lower than the replacement, repair or rebuild costs. People are most commonly underinsured because:
  - the policy sum insured does not necessarily increase annually, despite premiums increasing annually;
  - the consumer, or the insurer's sum insured calculator, underestimate the replacement, repair or rebuild costs; and/or
  - changes to building and planning requirements result in higher repair and rebuild costs, for example, to reduce bushfire risks.
- People usually only discover that they are underinsured when they make an insurance claim. The impact of underinsurance on their lives can be dramatic.

Sum insured issues

- It is very difficult, if not impossible, for a consumer to decide and then rely on the 'sum insured' amount for their home insurance policies. Online sum insured calculators are unreliable. What is included in the sun insured amount varies across policies.

- Determining an appropriate sum insured amount can be made more complex where the way a natural disaster impacts a building creates additional costs, such as 'make safe' costs. Whether these costs count toward the total sum insured is not consistent across different policies. It is sometimes not even necessarily clear how these costs will be treated from a reading of the policy. We have assisted consumers in cases where insurers have taken positions on the handling of these costs that we considered to be unreasonable.
- For example, in one case the home of a consumer who had combined home and contents insurance was damaged beyond repair by a natural disaster. The insurer sought to recover some of the contents from the house, but in order to do so, had to conduct 'make safe' works on the property. The insurer initially sought to deduct the cost of the 'make safe' works from the already insufficient sum insured.
- As detailed below in part 2f., where natural disasters are becoming more common, the cost of repairing or replacing insured assets can increase. These increases may be due to a range of factors, such as increased demand for the service in the time following a natural disaster, increased costs of supplies, or other increases in costs, such as changes to building codes requiring properties to be more disaster resilient.
- These can costs fluctuate significantly in the wake of disasters, which makes choosing the right sum to insure an asset for very difficult.

- **Case study**: Sophie (name changed) had home and contents insurance for her home in the outer suburbs of Melbourne. Sophie contacted her insurer to review the building sum insured for her property following the 2009 bushfires. Sophie told us that the insurer increased the building sum insured, with Sophie understanding this to mean that the new amount would provide sufficient coverage for her property on an ongoing basis. In 2016, a storm damaged Sophie's home, leaving it beyond repair. It was only at this point that Sophie told us that she learned the sum insured was insufficient to rebuild the house.

- We understand that insurers have taken some minor steps to address underinsurance, for example placing reminders to 'check your sum insured' in communications to policy holders. However, considering the devastating consequences that underinsurance has on families across Australia, in our view insurers can and should do much more to determine the appropriate sum insured for a customer, review this at renewal time and make the appropriate sum insured clearer to their customers.
- In recent years, many insurers have moved away from offering total replacement building insurance policies. The reasons for this should be examined and interventions considered to encourage more insurers to offer these policies. This would reduce the risk of under-insurance.
- The resolve problems with 'sum insured' issues, we recommend:

- **Recommendation 4**: Requiring insurance providers to disclose the costs that count towards the sum insured estimate, such as debris removal, demolition, and professional costs – policies vary on these inclusions.
- **Recommendation 5**: Requiring sum insured calculators to provide a transparent basis for their calculations, and for inputs to be obtainable by consumers in the event of a dispute about underinsurance.
- **Recommendation 6**: Explore barriers to total replacement building insurance policies, and address these to make this type of insurance more widely available.

- We note there are also issues with over-insurance in the home insurance market. In a recent study of pricing differences, the NSW ESLIM found 'data for a number of insurers in the study point to a clear practice of escalating the sum-insured on renewing policies each year. Increasing the sum insured each year can be important as a way to avoid under-insurance, but over-insurance can also be a problem for consumers.'[11] This is due to the increased premiums usually paid when a sum-insured is automatically adjusted upwards every year.

Underinsurance or non-insurance due to cost of premiums

- While some people might intentionally choose to reduce coverage, more often we see people take out insurance for a sum insured smaller than that necessary to properly mitigate their potential loss because they

[11] NSW ESLIM, *Pricing differences: New vs existing customers - Discussion Paper*, November 2018, p 6: https://www.eslinsurancemonitor.nsw.gov.au/sites/default/files/DiscussionPaper_Pricing_New%26Renewals_FINAL.pdf.

cannot afford the higher premium for complete cover. It might mean that if they incur significant damage or loss to the insured item, they will be left short, and unable to get themselves back on their feet if they incur significant losses.

- We are concerned that rising insurance premiums in areas at greater natural disaster risk will lead to consumers being forced into this situation. This could leave consumers extremely vulnerable. If this becomes the norm across a natural disaster-prone region, it could leave the whole community significantly exposed to risk.
- The prevalence of non-insurance is also only likely to increase as premiums become increasingly unaffordable in disaster-prone areas.
- In its second interim report, the ACCC Inquiry published information about non-insurance in northern Australia. It reported that the area had a significantly higher rate of non-insurance than the rest of the country, and that in general the cost of insurance was the main reason for non-insurance.[12]
- The likely outcome of this trend is that the communities most likely to be generally underinsured or uninsured are those where the natural disaster risk is higher, and financial wellbeing is lower.

Lower value alternative insurance products

- Exclusions from coverage is another form of underinsurance, where consumers purchase insurance products that limit coverage, whether the consumer knows it or not. Alternative products are becoming more common in the market and take different forms but will generally leave the insured party bearing an aspect of risk.
- Coverage might be limited with specific exclusions for certain types of loss. For example, a policy might exclude coverage for losses resulting from certain natural disasters, such as floods. We understand that insurance providers are also considering alternative forms of limited policies, such as those where a basic kit home might be provided to the insured, where a home is too costly to repair.
- We recognise that in some areas where high risk makes full coverage insurance unfeasible, these may be viable options. However, these products should not be sold unless there is a proven and genuine benefit to consumers. For example, there are claims ratios akin to other core insurance policies.
- It is essential that the development and sale of these types of policies be closely overseen by regulators for a number of reasons:
    - As discussed at Part 2c. above, there is significant risk consumers may not properly understand the exclusions in the policy.
    - Where consumers do understand the exclusions, they might still be purchasing policies that do not offer value for money. Consumers might purchase insurance products to protect themselves from specific risks they perceive to be significant, but their perception on this might be skewed due to behavioural factors or industry marketing. There is an information asymmetry between consumers and insurers, with insurers offering these products at a price determined based on a detailed calculation of risk, from which they consider themselves likely to make a profit.
    - As noted above, in natural disaster-prone areas, the risk of disaster often makes up a significant portion of a premium price. This will likely limit the amount that prices will be reduced for products that provide genuine cover for the disaster(s) that poses the greatest risk.
    - Under a product that offers alternative coverage (such as replacement with a kit home), insurers are more likely to decline to repair an insured house that could be repaired, because the alternative solution might be cheaper for them, even if it is a worse outcome for the insured.
- The insurance industry has a chequered history when it comes to selling alternative insurance products. There are a number of forms of insurance we consider to be ‘junk’ products, that offer little value to consumers. We have concerns that alternative low value forms of home or car insurance will be sold that are similarly designed to see consumers pay far more in premiums than will be paid in claims.

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[12] ACCC Inquiry, *Second Interim Report*, December 2019, p111-116.

e. re-insurance

- We are aware that reinsurance arrangements can significantly impact the terms, pricing, and availability of insurance cover. However, we do not have sufficient casework experience on the impacts of reinsurance arrangements to comment in detail in response to this Notice.
- We refer to Commission to the ACCC Inquiry's comments on reinsurance.

f. settlement arrangements, including cash settlements

- Under a home building insurance policy, an insurer can typically settle a claim for a cash amount, rather than arranging for building work to be done. The problems people face with cash settlements include:
  - clauses that allow the insurer to settle for an inadequate amount, such as the amount it would cost the insurer to rebuild, with their industry discounts which are not available to individual customers,
  - feeling pressured to accept cash settlement offers—often quickly—without knowing whether the offer is adequate to complete the work, and
  - feeling that they have been forced to accept cash settlement offers when they would prefer the insurer to undertake the work. This is a particular problem in remote areas, where it is difficult to find tradespeople to undertake the work.
- Home and contents insurance policies are more commonly operating under a 'sum-insured' model, rather than a policy allowing for complete repairs or rebuilds. Further, even under most policies offering complete repair or rebuild, the method by which a claim can be settled will include a cash settlement option alternative for all or part of a claim.
- This was an issue identified by the Financial Services Royal Commission in relation to the AAMI Complete Replacement Cover Policy. The FSRC identified that AAI (the product issuer) may have made false or misleading representations by promoting that AAMI would repair or rebuild an insured's house, no matter the cost, where AAI could choose to provide a cash settlement under the terms of the contract.[13]
- Cash settlements are sometimes necessary where repair or replacement is impractical, and in some cases might be preferable for all involved. However, we are concerned that insurers have acted unfairly in the application of cash settlement clauses, and have used them inappropriately.
- The amount to be paid under a claim was the most common issue raised in general insurance disputes before Australian Financial Complaints Authority (**AFCA**) over its first 12 months.[14] We consider this issue to be as important, if not more so, where claims relate to large scale natural disasters.

Cash settlements paid at the cost to the insurer

- The way a cash settlement figure is determined under the terms of a policy can leave people with inadequate funds to rebuild or repair their home after a disaster. A number of large insurers use standard terms in their home building insurance policies giving them broad powers to determine a cash settlement figure based on the lowest quote they obtain for the repairs. These clauses specify that the insurer will pay the figure it would cost the insurer to repair or replace the building—not the consumer.[15]
- Insurers have a commercial bargaining power advantage which allows them to engage builders to repair properties at lower rates—rates far lower than a consumer is able to obtain from a builder. Cash settlements subsequently reflect this lower amount. We have significant concerns that these terms are leaving people short. Further, people who are recovering from a disaster might feel extra pressure to take any amount offered where their life has been significantly disrupted.
- In addition, accepting a cash settlement means that people lose any guarantees by the insurer on the quality of the repair or rebuild works. The consumer is then left only with their standard protections against the builder or professional engaged.

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[13] FSRC, *Final Report: Volume* 2, page 441: https://www.royalcommission.gov.au/sites/default/files/2019-02/fsrc-volume-2-final-report.pdf.
[14] AFCA, *Snapshot of the first 12 months*, https://www.afca.org.au/news/statistics, accessed 7 April 2020.
[15] See for example, AAMI, Allianz.

- In our view, terms allowing insurers to pay a cash settlement amount based on what it would cost the insurer to repair or rebuild, are unfair contract terms. We note that the existing unfair contract regime will apply to standard form contracts subject to the *Insurance Contracts Act 1984* (Cth) from 5 April 2021, following legislation earlier this year implementing recommendations from the Financial Services Royal Commission (**FSRC**). Under this reform, from 5 April 2021, unfair contract terms in standard form insurance contracts will be void. We expect insurers to be proactively removing unfair terms from their policies, however unfair terms are not voided in an individual contract until they are challenged in a court or tribunal. It would be preferable if unfair contract terms were unlawful, with civil penalties applying for any breach.[16]

Increased costs following a natural disaster

- The other concern we hold over cash settlements specifically in relation to natural disaster related claims, is the availability of repair and building services immediately following a disaster. After a natural disaster there is increased demand for building and other trade services. This can increase the prices quoted and lead to delays and difficulties in engaging qualified repairers quickly.

- Further, where an area has become more fire prone over time, new fire safety rules and building codes may apply, increasing the general costs of rebuilding. This can particularly increase the costs of repairing older homes that are damaged by bushfires.

- This means that even where a cash settlement might be made at a fair estimate that would ordinarily allow the consumer to repair or replace the building insured, the increased costs resulting from the disaster might still leave them short, or result in significant delays for the repairs.

Impact of rights of mortgagees

- Cash settlements can also pose an additional problem to people affected by natural disasters who have mortgages. Where there is a mortgage on the damaged property, the mortgagee is normally entitled to receive the insurance payout and then approve any repairs done on the property. This can leave the landowner with little or no power in the repair process, despite being the party insured and the one directly impacted.

- **Case study:** Lucy (name changed) made a claim under her home and contents insurance after her home burned down in Northern Victoria in 2019. Lucy told us that it took 6 months from when she first lodged her claim for a cash settlement for the contents aspect of her claim to be paid, and 10 months for the insurer to agree on a cash settlement for the home itself. Lucy reported that the insurer made the whole claims process difficult to navigate. She told us that there were significant unexplained delays, she was repeatedly asked for the same documentation, and she had to repeatedly contact the insurer to seek information about progress and important documents.

- The cash settlement figure for the home to be rebuilt was roughly $150,000 more than Lucy owed on her mortgage. The insurer contacted the lender to ask whether the settlement amount could be paid to Lucy in full, or whether a portion must first be paid to discharge the mortgage.

- Lucy told us that her lender had requested the insurer pay the full cash settlement amount directly to them (including the approximately $150,000 more than was owed on the mortgage), despite already indicating her intention with the lender to discharge her mortgage. Lucy contacted us and sought our advice, having been told by her insurer that she needed to work this out with her lender, as the insurer required the consent of the lender to pay out the claim.

- Lucy was happy for the portion of the settlement payout necessary to discharge her mortgage to go to the lender, but rightfully wanted any additional amount to be paid directly to her. Lucy told us that she eventually got the outcome she wanted and received the settlement amount left over after discharging her mortgage directly, but only after she told her lender that their request to receive the whole sum was unlawful.

[16] This option is being considered by consumer affairs officials, see: https://consult.treasury.gov.au/consumer-and-corporations-policy-division/enhancements-to-unfair-contract-term-protections/. Consumer Action's submission to the consultation is available here: https://consumeraction.org.au/treasury-consultation-enhancements-to-unfair-contract-term-protections/.

- While we understand that Lucy's fire was not caused by a bushfire, her experience is an example of the problems that can occur with claims handling and cash settlements following natural disasters, particularly in regional areas.

g. claims-handling

- From a consumer perspective, claims handling is one of the most critical parts of the insurance process, but often tends to be the most problematic. In relation to natural disasters, people will usually be making claims for assistance that they desperately need while in extremely vulnerable circumstances. Unfortunately, significant issues with the way general insurers handle claims have been consistently reported by consumers. ASIC has recently taken enforcement action against Youi relating to its claims handling following a severe hailstorm.[17]

Claims handling currently not overseen by ASIC

- Poor conduct by insurers in claims handling has been difficult to stop or address because the handling of claims has been excluded from the definition of a 'financial service' under the *Corporations Act 2001* (Cth). This excludes the handling of insurance claims from the same regulatory oversight applied to insurance policies and advice.

- The removal of this exclusion was recommended in the Final Report by the FSRC, and would bring claims handling within ASIC's oversight.[18] Treasury released Exposure Draft Legislation for consultation in late 2019.[19] However, legislation has not yet been introduced to Parliament.

- Regulating insurance claims handling as a financial service would require insurers to handle claims efficiently, honestly and fairly—which is a bare minimum that people should be able to expect from their insurers. Currently, the regulator can only take action in relation to claims handling where it breaches the duty of utmost good faith (see footnote 15 above). While good faith arguably requires insurers to investigate claims in a reasonable manner, to administer claims efficiently and without delay, and to not use inappropriate reasons to deny claim, applying the fairness duty to claims handling will provide ASIC with much greater power to meet community expectations.[20]

- We have long seen consumers' claims handled in ways that fall far short of this bar—there is a real need for insurers to be legally obliged to handle claims appropriately. While we understand that COVID19 might result in some delays in implementing the FSRC reforms, making this change is uncontroversial and important. We encourage the Royal Commission to recommend that this reform be legislated as a matter of urgency.

Delays in assessment

- As noted above in Part 1 to this response concerning the handling of claims, we have heard reports from regional community groups that there have been significant delays for some residents in having home building insurance claims assessed for damages caused by the 2019-20 bushfires.

- This is a relatively common issue in the aftermath of natural disasters. Obviously where there are spikes in the volumes of claims being made, insurers will have some logistic difficulties in assessing claims, particularly in regional areas.

- However, any delays at this point slow the whole repair process significantly, as it is a necessary first step before the claim can be progressed. This leaves the person making the claim in a vulnerable situation causing great uncertainty, where they are relatively powerless. Where the policyholder requires emergency accommodation, they have no certainty about whether their costs will be reimbursed prior to the assessment. Further, where 'make safe' works are required on a property, the delay leaves the occupants of that property exposed to harm.

- A number of the insurance case studies in Volume 2 of the Final Report by the FSRC concerned delays in finalising assessments for natural disasters. In those cases, delays often occurred because of the time it took

[17] ASIC, *ASIC commences proceedings against Youi Pty Ltd for alleged breaches of the duty of utmost good faith*, 16 April 2020: https://asic.gov.au/about-asic/news-centre/find-a-media-release/2020-releases/20-091mr-asic-commences-proceedings-against-youi-pty-ltd-for-alleged-breaches-of-the-duty-of-utmost-good-faith/.
[18] Recommendation 4.8.
[19] The Treasury, *Making insurance claims handling a financial service – Exposure draft legislation*, 29 November 2019: https://treasury.gov.au/consultation/c2019-36687.
[20] For more information, see https://consumeraction.org.au/20190409-insurance-claims-handling/.

for the insurer's representative to attend the property, and for the right expert to attend the property and prepare a report.[21]

Repair process issues

- Delays in actually delivering repairs in the wake of natural disasters can also cause significant detriment to those impacted. This is to some extent unavoidable at times, such as where a remote region is significantly impacted by a natural disaster and availability of builders is limited.
- This is an issue which is unfortunately only likely to get worse as the frequency and severity of natural disasters increase.
- There are also instances however where claims management practices can cause additional delays in the delivery of a proper outcome for policyholders. We consider this to be an area that improvements can and should be made. Insurers at times will cause delays where they:
  - dispute what needs to be done;
  - are unwilling to seek alternative service providers where their preferred providers are booked out; or
  - elect to seek, and go with, lower quotes for repairs.
- The other issue that commonly arises involves poor quality repairs. Where a job is not done properly in the first instance, this can result in ongoing problems for families living in a property. This issue can also be more common where natural disasters result in higher demand for the relevant specialists in the region, and getting to the next job takes precedence over quality.
- A number of these issues came to light in the FSRC and can be seen in the case studies in Volume 2 of the Commission's Final Report, concerning Youi and AAI.[22]

Unregulated claims management services

- Insurance claims management services are for-profit businesses that represent policyholders for a fee, to undertake the administrative work on an insurance claim. Claims management services typically work for a percentage of any cash settlement offered by the insurance company.
- The industry is currently not subject to any specific regulation or oversight. Insurance claims management services are not required to hold an Australian Financial Services Licence nor are they regulated under the *Australian Securities and Investments Commission Act 2001* (**ASIC Act**). They therefore do not have to be members of external dispute resolution scheme like AFCA, or have any training or conduct requirements. This leaves policyholders with limited avenues for redress in the event of a dispute with an insurance claims management service. Disputes taken to court are generally time consuming, difficult and costly to resolve compared to AFCA.
- Insurance claims management services can increase the risk of poor outcomes for the policyholders they represent, insurance companies and other policyholders due to their fundamental conflicts of interest. It is in the financial interests of insurance claims management services to seek a cash settlement as a resolution rather than getting the insurer to repair or rebuild the damaged property, because their fee is generally a percentage of the cash settlement.
- During the 2019-20 Australian bushfire crisis, ASIC released a statement warning consumers away from using "unscrupulous service providers".[23] While those impacted by natural disasters might think it prudent to engage a service that holds itself out as an expert in this area to handle such an important claim, they might be left worse off for doing so. Where large scale natural disasters occur, these services are also likely to appear more attractive to policyholders, who might be facing delays in having their claims assessed due to an increased number of claims.

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[21] FSRC, *Final Report Volume 2: Case Studies*, Part 9.2.2, Glenn Sutton, p 421; Part 11 AAI Ltd (Hunter Valley Storm), p 445.
[22] See FSRC, *Final Report Volume 2: Case Studies*, Part 9.2 Youi, Evidence, p 416; Part 11 AAI Ltd (Hunter Valley Storm), p 445 https://www.royalcommission.gov.au/sites/default/files/2019-02/fsrc-volume-2-final-report.pdf.
[23] ASIC, *ASIC encourages fair and effective insurance claims handling for people affected by the bushfires – warns against unscrupulous "service providers"*, 9 January 2020: https://asic.gov.au/about-asic/news-centre/find-a-media-release/2020-releases/20-006mr-asic-encourages-fair-and-effective-insurance-claims-handling-for-people-affected-by-the-bushfires-warns-against-unscrupulous-service-providers/.

- **Recommendation 7**: Insurance claims handling should be defined as a 'financial service' and subject to the general AFSL holder obligations under section 912A of the Corporations Act. Regulation of claims handlers should include for-profit third party 'claims managers' purporting to act for the consumer.

h. suitability of insurance products

- Unlike in other jurisdictions like the United Kingdom, there is no legal requirement to ensure insurers and insurance brokers sell suitable products.
- Insurance might be unsuitable because it does not cover a risk that the consumer needs to cover—for example a home building policy without flood cover sold to someone in a flood-prone area.
- The recent 'design and distribution obligations' are an important consumer protection but do not go as far as requiring that a particular product be suitable for the particular individual is it sold to.
- A robust suitability requirement, with consequences for breach, would mean insurance products are suitable for people and perform as expected, avoiding claim shock and inappropriate coverage.

i. consumers' ability to compare and choose appropriate insurance coverage

Failures of disclosure

- The current disclosure regime for insurance often means little more than a financial services entity providing a Product Disclosure Statement (**PDS**) of many of dozens of pages to the customer. This type of disclosure is increasingly being recognised as an outdated and ineffective form of consumer protection—it assumes that people make rational decisions on all the available information, and does not acknowledge the realities of human behavioural biases.[24] The complex nature of financial products, particularly insurance, means that a disclosure approach has significant limitations.
- It is now well-established that insurance disclosure, through PDSs and Key Fact Sheets, is ineffective.[25] The Insurance Council of Australia's own research found that 8 out of 10 people not read the PDS.[26] ASIC found that the age of disclosure as the primary consumer protection in financial services is over.[27]
- As the cases studies of Allianz, AAI and CommInsure at the FSRC showed, the problem is not the disclosure regime alone. It is also advertising—an effective and engaging form of product disclosure—which can mislead people as to the key features of products. In addition, sales scripts and practices, such as those seen in the ClearView and Freedom case studies, can also mislead people and inhibit them from deciding whether a product would be suitable for them. The disparity between sales pitch and reality further undermines the disclosure regime.
- The most effective changes that could be made to achieve the objective of better consumer understanding and choice of financial products are:
    - A modernised standard cover regime for insurance, to provide a minimum standard that meets community expectations. For complex products such as insurance, standardised products are needed to improve the effectiveness of disclosure.
    - A requirement to include on insurance renewal notices the components of the premium and that of the prior year, as recommended by the Senate Economics References Committee[28] and as implemented in New South Wales. Disclosure of the prior year's premium has been shown to be

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[24] See for example ASIC, *Submission: Senate Economics References Committee Inquiry into Australia's general insurance industry*, March 2017, p 12.
[25] See for example Justin Malbon and Harmen Oppewal, *(in)Effective Disclosure: An experimental study of consumers purchasing home insurance* (2018): https://australiancentre.com.au/wp-content/uploads/2018/09/InEffectiveDisclosure-final.pdf; Senate Economics References Committee, *Australia's general insurance industry: sapping consumers of the will to compare* (2017); Insurance Council of Australia, *Consumer Research on General Insurance Product Disclosures: Research findings report*, February 2017: http://www.insurancecouncil.com.au/assets/report/2017_02_Effective%20Disclosure%20Research%20Report.pdf.
[26] ICA, *Consumer Research on General Insurance Product Disclosures: Research findings report*, February 2017, p 18.
[27] ASIC, *Rep 632: Disclosure: Why it shouldn't be the default A joint report from the Australian Securities and Investments Commission and the Dutch Authority for the Financial Markets*: https://download.asic.gov.au/media/5303322/rep632-published-14-october-2019.pdf.
[28] Senate Economics References Committee, *Australia's general insurance industry: sapping consumers of the will to compare*, August 2017, ix (rec 3 [3.76] rec 4 [3.77]).

effective in prompting people to 'shop around'.[29] The renewal notice should also include an updated sum insured estimate.

  - A suitability test for insurance, which would consider claims ratios, eligibility targets and compliance performance of insurance products. This could be formulated with consideration of the UK's individual suitability test.[30] The design and distribution obligations, in the process of being implemented, are not an individual suitability requirement.

The need for a modernised standard cover regime

- The current 'standard cover' regime prescribes certain insurance contracts (including home, motor vehicle and travel) and specifies the standard cover, events, exclusions and minimum benefits under those contracts.[31]
- Standard cover was introduced after the Australian Law Reform Commission (**ALRC**) reported in 1982 the need for fair competition and informed consumer choice in insurance. The ALRC's report recommended 'standard cover' for certain types of domestic insurance, 'to prevent insureds being surprised by unusual terms in major fields of domestic insurance'.[32] The ALRC reasoned that:

  > The market at present is distorted by the fact that purchaser discrimination is limited to matters like price, little or no account being able to be taken of differences in the nature of the products being sold… Policies contain numerous terms which affect in unexpected ways the cover offered… The insured's ignorance remains undisturbed until he (sic) makes a claim.[33]

- However, an insurance policy can provide less than standard cover if:
  - the insurer 'clearly informed the insured in writing (whether by providing the insured with a document containing the provisions, or the relevant provisions, of the proposed contract or otherwise)', or
  - 'the insured knew, or a reasonable person in the circumstances could be expected to have known' that the insurance contract provided less than the standard cover, or no cover.[34]
- The way standard cover is formulated, an insurer can inform a consumer that terms offer less than standard cover in various ways, including in the Product Disclosure Statement (**PDS**), without drawing attention to the terms in question.[35]
- It is fair to say that standard cover is not a reality. We have no minimum standard for insurance and no benchmarks for comparison. After 30 years, the standard cover regime has not had the impact on the market that the ALRC intended.
- The way the standard cover regime has been formulated puts the onus on consumers to choose insurance which suits them, by navigating PDSs which are long, complex and jargon-filled, and which vary significantly between insurers. The standard cover regime relies on consumers knowing what standard cover looks like, and what they should expect from their insurance. However, there is extremely low public awareness that standard cover even exists. There are no accessible, consumer-focused resources on standard cover.[36]
- A 2017 review by Consumer Action of home building, home contents and comprehensive car insurance offered by five major Australian insurance brands found:

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[29] Financial Conduct Authority, *FCA to require insurance firms to publish details of last year's premium*, 3 December 2015: https://www.fca.org.uk/news/press-releases/fca-require-insurance-firms-publish-details-last-year%E2%80%99s-premium.
[30] Financial Conduct Authority, *Insurance Conduct of Business Sourcebook,* Release 32 (2018), ch 5: https://www.handbook.fca.org.uk/handbook/ICOBS/5.pdf; Gail Pearson, 'There are a few gaping holes in the proposals to beef up ASIC', *The Conversation* (Online), 16 December 2016: https://theconversation.com/there-are-a-few-gaping-holes-in-the-proposals-to-beef-up-asic-70408.
[31] The prescribed contracts under the standard cover regime are motor vehicle insurance, home building and home contents insurance, sickness and accident insurance, CCI and travel insurance: *Insurance Contracts Regulations 1985* (Cth) Pt 5. For insurance which sits outside the standard cover regime, insurers must disclose any 'unusual' terms in a similar way to the standard cover requirement: Insurance Contracts Act s 37.
[32] ALRC, *Report No 20: Insurance Contracts*, 1982, p xxii.
[33] ALRC, *Report No 20*, paras 69-70.
[34] *Insurance Contracts Act 1984* (Cth) s 35(2).
[35] See Mann, *Mann's Annotated Insurance Contracts Act*, 6th ed, 2014, Lawbook Co, para 35.30.
[36] We could not find reference to standard cover on ASIC's MoneySmart website (moneysmart.gov.au), and the Insurance Council of Australia's Understand Insurance site (understandinsurance.com.au) does not explain standard cover, both accessed 20 April 2020.

- none of the home building or home contents policies provided standard cover,[37] and
- one of the comprehensive car insurance providers appears to offer standard cover, however this analysis is complex and uncertain.[38]

- Standard cover is rarely raised by consumers in disputes with insurers. When it is raised, it appears to provide little recourse for consumers. Consumer Action reviewed Financial Ombudsman Service (**FOS**) decisions between 1 July 2013 and 30 June 2018. This review found that, of the thousands of FOS domestic insurance determinations since July 2013:
  - standard cover was considered in just 30 determinations;
  - standard cover was found to apply in 43 per cent of those cases; and
  - the insurer had not provided a PDS in 92 per cent of cases where standard cover applied—that is, the insurer's failure to provide a PDS is the overwhelming reason standard cover applied.
- The experience of consumers at EDR indicates that standard cover is rarely raised by consumers in disputes with insurers, and when standard cover is raised, it appears to provide little recourse for consumers.
- The Federal Government's 2019 review of standard cover appears to have stalled after the release of a discussion paper.[39] Other reforms to general insurance will be ineffective until standard cover is modernised to enable people to compare and understand their home and car insurance. Options and issues which should be considered are:
  - Updating the features of the existing standard cover regime[40] to meet modern community standards and expectations. It is unlikely that a regime developed without significant consumer input in the early 1980s is fit for purpose today.
  - Making standard cover a mandatory minimum standard for insurance policies.
  - Developing a 'rating' system which rates products against the standard cover benchmark.
- The highly variable cover and inconsistent definitions are notable and surprising given the general insurance market in Australia is highly concentrated. As the FSRC found, AAI alone issues 37 home and contents insurance products through 13 different brands, including AAMI.[41]

- **Recommendation 8**: Progress the Government's review and modernisation of standard cover.

The need for standardised definitions

- The wording and coverage of insurance policies vary hugely. This makes the task of comparing policies and making an informed choice virtually impossible. As the Federal Treasury observed:

> Insurance contracts that are required to include the same terms and conditions may still deliver variable levels of coverage, if the terms of the contract do not rely on a standard definition. Inconsistent definitions between policies risk misleading consumers into thinking they have cover for certain events when they do not.[42]

- Inconsistent definitions mean people are confused, or misled, into thinking they are covered for events and risks that they are not, based on technical wording and fine detail buried in policies that people do not read and may not understand.
- In August 2017, the Senate Economics References Committee Inquiry into Australia's general insurance industry reported that the complexities and variations in home and motor vehicle insurance were 'sapping

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[37] All home building and contents policies reviewed excluded actions of the sea. Landslide, subsidence and erosion were excluded except in certain circumstances. Flood was often optional. Standard cover for home building and home contents would insure all of these risks.
[38] Four policies appeared to offer a narrower range of cover where a person other than the insured was driving the car, with the insured's permission, and incurred liability to a third party. Others excluded damage or loss to standard accessories, which are covered under standard cover.
[39] The Treasury, *Disclosure in General Insurance: Improving Consumer Understanding – Discussion Paper*, 15 January 2019: https://treasury.gov.au/consultation/c2019-t354736.
[40] Insurance Contracts Regulations 2017 (Cth), pt 3 div 1.
[41] FSRC, *Final Report: Volume 2*, p 433: https://www.royalcommission.gov.au/sites/default/files/2019-02/fsrc-volume-2-final-report.pdf.
[42] The Treasury*, Disclosure in General Insurance: Improving Consumer Understanding, Discussion Paper*, January 2019, p 16.

consumers of the will to compare'.[43] The varied definitions of key terms is a significant part of this failure in the market. Examples of this include:

  - There are different definitions of 'actions of the sea' under home insurance policies, which exclude loss or damage caused by 'actions of the sea' to a greater or lesser extent.[44]
  - There are different definitions of the 'reasonable cost' for which insurers will cash settle a home building claim.[45]

- The importance of definitions in insurance policies became very clear in 2011, when major flooding in Queensland saw some people's claims denied because the definition of 'flood' in their policy did not include riverine flooding.[46] The Government responded by legislating a standard definition of 'flood' in home, strata and some small business insurance contracts, which includes riverine flooding.[47] We understand that the standardised definition of 'flood' has reduced the likelihood of dispute about whether damage is caused by a floor or not.
- The recent report by CHOICE details the problems with inconsistent definitions.[48] CHOICE found that "fire cover" is a standard inclusion in home and contents insurance, but what a consumer is covered for is defined in many different ways. A consumer might think they have a valid insurance claim from the Black Summer bushfires, but it will depend what policy they have whether they are covered for damage on property that was directly affected by bushfire or indirectly affected. Were there flames on the property? Was the damaged property just scorched, but not burnt to the ground? Did the consumer only suffer smoke damage? Was the home only partially burnt or were there valuable items that melted? This lack of standardised terms among insurers means claims can be open to interpretation and can leave consumers underinsured and in shock when they make a claim.
- The Senate Economics References Committee Inquiry recommended the government work closely with industry and consumer groups to establish standard definitions of other key terms in general insurance policies.[49] In our view, this should extend to life insurance policies, as the same problems and principles apply across many types of insurance policies.

- **Recommendation 9**: Standard definitions of key terms in life and general insurance policies should be defined at law and should be developed in consultation with stakeholders, including consumer groups.

Sales practices

- Insurers' desire to cross-sell additional insurance policies to their existing customers is strong. This bundling, often tempting through the use of sign-up discounts, can led to detriment due to the 'loyalty tax' and later difficulties in switching to a cheaper deal form another insurer.
- The FSRC made a number of critical recommendations to sales practices for insurers, including a ban on the unsolicited selling of insurance, introducing a deferred sales model for add-on insurance, regulating claims-handling, converting the insured's duty of disclosure to a duty not to make a misrepresentation, and a ban on conflicted remuneration for insurance. These reforms were largely due to be tabled in Federal Parliament by 30 June 2020[50] but have been delayed by the COVID-19 crisis.
- It is of critical importance that these reforms are passed as a matter of urgency.

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[43] Senate Economics References Committee, *Australia's general insurance industry: sapping consumers of the will to compare* (2017).
[44] CHOICE, cited in Senate Economics References Committee, *Australia's general insurance industry: sapping consumers of the will to compare* (2017), 38, [3.62].
[45] See for example AAMI, *Home Building Supplementary Product Disclosure Statement* (19 January 2018): https://www.aami.com.au/aami/documents/personal/home/spds-building-05-03-2018.pdf; *RACV, Home Insurance: Product Disclosure Statement and Policy Booklet* (29 September 2017), 71: https://www.racv.com.au/content/dam/racv/documents/insurance/racv-home-insurance/RACV_Home_PDS_G018333_0618.pdf; Allianz, *Home Insurance Product Disclosure Statement* (31 May 2017), 6: https://www.einsure.com.au/wb/public/openCurrentPolicyDocument/POL1085DIR/$FILE/POL1085DIR.pdf.
[46] See Treasury, *Reforming Flood Insurance: Clearing the Waters* (2011), p 3–4.
[47] *Insurance Contracts Regulations 2017* (Cth) r 34.
[48] CHOICE, Andy Kollmorgen, *How does your insurer define a fire?* Choice.com.au, 6 February 2020: https://www.choice.com.au/money/insurance/home-and-contents/articles/fire-definitions-by-insurers.
[49] At ix (rec 6 [3.79]).
[50] The Treasury, *Financial Services Royal Commission Implementation Roadmap*, 19 August 2019: https://treasury.gov.au/p2019-399667.

- **Recommendation 10**: Progress the outstanding FSRC reforms to insurance, including a ban on unsolicited selling of insurance, a deferred sales model for all add-on insurance, and reforms to the duty of disclosure.

3. **From the perspective of the Consumer Action Law Centre, is there any necessity for additional Commonwealth assistance and/or intervention e.g. in initiating regulatory investigations, setting national standards, assisting in the establishment of self-insurance scheme (independently of current ASIC and APRA programs and initiatives).**

Insurance pricing monitor

- We strongly support the work of the ESL Insurance Monitors in NSW[51] and previously in Victoria. The mandate for state-based regulators to obtain and analyse pricing data has been invaluable to identify and address the consumer harm from insurers' pricing strategies and potential price exploitation.
- There are transparency issues underlying affordability concerns. Consumers do not have access to the information that insurers use in making pricing decisions. A permanent price monitor, properly resourced and empowered, could improve transparency including understanding of the determinants and make-up of insurance policy premiums.
- Insurers should welcome greater scrutiny of their pricing practices, which can improve trust and competition in an industry beset by scandals following the FSRC.
- Regulators will need to play an important role in tracking home and contents insurance rates after the Black Summer. Areas affected by recent bushfires will likely be subject to an adjustment of reinsurance rates and a subsequent increase in insurance premiums for homeowners.
- In addition to pricing data, regulators will need to obtain, analyse and ideally publish the following data:
    - rates of opting out from fire coverage in bushfire-prone areas and other downgrades in coverage (i.e watch for a trend similar to flood opt-out rates in Northern Australia);
    - premium increases for home and contents insurance in bushfire prone areas;
    - non-payment of premiums, rate of lapsed or cancelled policies, which may indicate affordability problems and poor financial hardship responses from insurers; and
    - rates of cash settlements after bushfire events, which may indicate financial hardship, particularly in light of COVID-19.

- **Recommendation 11**: Establish a federal insurance pricing monitor, based on the NSW and Victorian Emergency Services Levy monitors, or empower and resource the ACCC to undertake such functions on an ongoing basis.
- **Recommendation 12**: Implement a data monitoring program to analyse and publish rates of: fire coverage opt-outs; premium increases; lapsed policies and non-payment of premiums; cash settlement.

Community legal services funding

- It is an unfortunate reality that with more frequent and more significant natural disasters, an increasing number of Australians are going to experience financial hardship in their wake.
- The financial difficulties faced by people in the wake of natural disasters are complex and multifaceted. Natural disasters can cause short or long-term losses of income for those impacted, and at the same time create an acute need for money to help survive the disaster and its immediate aftermath. Community members might feel they have little option but to take on significant debt when they have little capacity to pay it back.
- Making lawyers with relevant financial services expertise accessible to those who cannot afford to pay for legal advice in the lead up to, and immediately after, natural disasters can help people get the advice they need to recover from disasters and enforce their consumer rights.

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[51] https://www.eslinsurancemonitor.nsw.gov.au/.

- However, there are significant limitations on the availability of these services. Community legal centres are already unable to meet the demand for their services. There is no buffer to absorb the increase in demand that arises from a natural disaster. Regional community legal centres need to provide legal expertise of all types, so when disasters hit, their capacity to provide consumer law, consumer credit and insurance-focused legal advice can be limited.
- As a community legal centre specialising in consumer law, consumer credit and insurance law, Consumer Action also cannot keep up with demand for our services at the best of times. In the last three years, email enquiries to our legal advice line have increased by 170%. These enquiries come directly from members of the public, as well as from other community workers and financial counsellors.
- There is urgent need for increased funding for community legal centres, including specialist consumer finance lawyers within community legal centres in Australia. This would enable community lawyers to directly help more individuals in need of legal assistance following natural disasters. It would also enable specialist community legal centres like ours to provide additional training and support to regional generalist community legal centres to prepare them to assist with insurance and other consumer law issues following a disaster.
- The FSRC explicitly recognised that '[t]he legal assistance sector and financial counselling services perform very valuable work. Their services, like financial services, are a necessity to the community.'[52] Commissioner Hayne also recognised that these services struggle to meet demand within current resourcing and found that: 'the desirability of predictable and stable funding for the legal assistance sector and financial counselling services is clear and how this may best be delivered is worthy of careful consideration. Such consideration should look at all options that may be available to supplement existing funding.' Commissioner Hayne is not the first to call for increased funding for legal assistance services. In its 2014 Access to Justice Inquiry Report, the Productivity Commission called for $200 million in annual funding for civil legal assistance services (Recommendation 21.4). The Commission acknowledged the need to fund strategic advocacy and law reform to reduce demand for front line services (Recommendation 21.1).
- The Government's formal response to the Final Report of the Royal Commission agreed with the need for predicable and stable funding for legal and financial counselling services. The Sylvan Review into funding for financial counselling services in 2019 noted that increasing the availability of financial counsellors as well as improving the visibility and reach of these services will also drive the need for legal assistance services.[53]
- However, we have only seen action from Federal and State Governments in relation to financial counselling funding. Governments have made no specific commitments in relation to specialist consumer or financial services legal assistance, despite the huge increase in demand for our services in recent years. There appears to have been little consideration about the impact on consumer credit and insurance legal services that will receive a significant increase in requests for legal advice from financial counsellors, or the need to adequately resource the integrated model which has proven to be effective.
- Lawyers work hand-in-glove with financial counsellors, through integrated services (each professional supporting aspects of a clients' problem). These working relationships create efficiencies in delivering access to justice. For example, lawyers can offer specialist support to financial counsellors, including training and secondary consultations. Such models have been shown to efficiently enhance access to justice.[54]
- The Government is currently proposing to fund community legal centres, including consumer credit and insurance specialist CLCs, through the National Legal Assistance Partnership (**NLAP**) from 1 July 2020. There is no additional funding proposed for consumer and insurance legal assistance, and the allocations do not keep pace with indexation or population growth, or the expected increased demand resulting from climate change and natural disasters.

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[52] FSRC, Final Report: Volume 1, p 491: https://www.royalcommission.gov.au/sites/default/files/2019-02/fsrc-volume-1-final-report.pdf.
[53] Australian Government Royal Commission Response, February 2019, page 39: https://treasury.gov.au/sites/default/files/2019-03/FSRC-Government-Response-1.pdf.
[54] Liz Curran, 'Multidisciplinary Practice Health Justice Partnerships: working ethically to ensure reach to the most in need' (2017) 26 *Nottingham Law Journal* 11-36.

- The community legal sector estimates that funding of $26 million per annum for an additional 200 specialist consumer, credit and insurance lawyers located in community legal centres across Australia is needed to meet demand.

- **Recommendation 13**: That the Government commits $26 million annual funding for community legal centres for an additional 200 specialist consumer, credit and insurance lawyers located in centres across Australia

Other issues within the Terms of Reference: Financial hardship

- Consumer Action's financial counsellors handle a majority of the Victorian calls made to the National Debt Helpline (**NDH**). The calls we receive from Victorians impacted by bushfires are rarely limited to insurance issues. In addition to insurance, we consider there to be other reforms needed to protect consumers from unscrupulous business practices in the aftermath of natural disasters.
- Following a natural disaster, we receive calls from people stressed and struggling to keep up with bills or other bills due to lost income, or extra costs caused by the disaster. This includes costs for utilities, telecommunications and repayments on debts and mortgages. Even where a community member does not suffer obvious losses to assets, they may still struggle to keep their head above water financially for a range of reasons.
- Keeping up with these payments should not be a significant source of stress for people in the immediate aftermath of natural disasters. Essential service providers such as energy, water, rental housing and telecommunications, should be required to give customers in impacted communities following natural disasters a reasonable grace period to catch up on bills. This should be a positive obligation that does not require contact by the customer where there is evidence to suggest a customer is in a disaster impacted area. After a disaster, it can be very difficult to contact service providers for a range of reasons.
- Similar obligations should be imposed upon banks, lenders and any other companies to which debts are owed. While essential service providers and lenders have hardship policies, they often fall short in substantive assistance offered or require proactive contact from the consumer. Where the area someone resides in is impacted by a natural disaster, the default response should see debts paused or deferred for a period sufficient for those impacted to deal with the immediate aftermath.
- Furthermore, predatory businesses such as payday lenders, consumer lease providers and 'debt vultures' offering debt management firms must be appropriately regulated. The *National Consumer Credit Protection Amendment (Small Amount Credit Contract and Consumer Lease Reforms) Bill 2019 (No. 2)* currently before Parliament would provide much needed additional protections to consumers in disaster-hit areas from predatory lenders. Finally, debt vultures must also be brought within the financial services regulatory framework to ensure they are providing appropriate advice to people in financial hardship.

Please contact Katherine Temple, Director of Policy and Campaigns, on 03 9670 5088 or at katherine@consumeraction.org.au if you have any questions about this response.

Yours Sincerely

CONSUMER ACTION LAW CENTRE

Gerard Brody

Gerard Brody | Chief Executive Officer

APPENDIX A – SUMMARY OF RECOMMENDATIONS

- **Recommendation 1**: An independent expert panel review insurance affordability in Australia, having regard to the rising levels of financial difficulty and the worsening impacts of climate change.
- **Recommendation 2**: Federal and state governments, the insurance industry, and consumer groups work together on an industry-wide response to the impact of climate change on the provision of insurance.
- **Recommendation 3**: Improve hardship protections in the insurance industry.
- **Recommendation 4**: Requiring insurance providers to disclose the costs that count towards the sum insured estimate, such as debris removal, demolition, and professional costs – policies vary on these inclusions.
- **Recommendation 5**: Requiring sum insured calculators to provide a transparent basis for their calculations, and for inputs to be obtainable by consumers in the event of a dispute about underinsurance.
- **Recommendation 6**: Explore barriers to total replacement building insurance policies, and address these to make this type of insurance more widely available.
- **Recommendation 7**: Insurance claims handling should be defined as a 'financial service' and subject to the general AFSL holder obligations under section 912A of the Corporations Act. Regulation of claims handlers should include for-profit third party 'claims managers' purporting to act for the consumer.
- **Recommendation 8**: Progress the Government's review and modernisation of standard cover.
- **Recommendation 9**: Standard definitions of key terms in life and general insurance policies should be defined at law and should be developed in consultation with stakeholders, including consumer groups.
- **Recommendation 10**: Progress the outstanding FSRC reforms to insurance, including a ban on unsolicited selling of insurance, a deferred sales model for all add-on insurance, and reforms to the duty of disclosure.
- **Recommendation 11**: Establish a federal insurance pricing monitor, based on the NSW and Victorian Emergency Services Levy monitors, or empower and resource the ACCC to undertake such functions on an ongoing basis.
- **Recommendation 12**: Implement a data monitoring program to analyse and publish rates of: fire coverage opt-outs; premium increases; lapsed policies and non-payment of premiums; cash settlement.
- **Recommendation 13**: That the Government commits $26 million annual funding for community legal centres for an additional 200 specialist consumer, credit and insurance lawyers located in centres across Australia