

# General Insurance Industry Reform

The following Submission whilst not directly addressing, the questions raised in the Northern Australian Insurance Inquiry issues paper document, does highlight several fundamental reform issues and introduce possible solutions. If these are understood and acted upon the issues raised by the enquiry paper will be significantly reduced.

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## **Introduction**

A strong and healthy General insurance Industry is an essential part of any economy but it has to be well regulated and monitored to ensure there is an appropriate balance between the Industry and the protection of consumers.

This has largely been achieved through the role of ASIC and in particular the introduction of the Insurance Contracts Act in 1986.

Legislation introduced post the Insurance Contracts Act (from a Consumer Protection point of view) has generally been ineffective and in some cases detrimental.

We are now in a position whereby the balance is weighted in favour of the Insurance Industry and whilst it may not be readily noticeable it is important that the contributing issues are addressed before they become larger problems.

## **Insurance Contracts Act**

The Insurance Contracts Act is a document that legislates an attitude, "Utmost Good Faith", a concept that forms the basis of every contract of insurance. The fact that there has been very little amendments introduced to the Insurance Contracts Act since its inception in 1986 is evidence of an enduring and well written piece of legislation.

The Act also performs a second, very important purpose by providing a "safety net" for consumers when purchasing an insurance product. This is achieved through the use of prescribed contracts. There are currently 6 prescribed contracts.

Home Building

Home Contents

Motor Vehicle

Travel

Loan Protection

Sickness and Accident.

These contracts detail a minimum or standard cover that is required in order to issue an insurance policy. The insurer can choose to provide less cover or no cover or pay a lesser amount for a claim, however in order to do so they must prove that they have clearly informed the insured that the cover is less than prescribed.

Originally this was done by way of a “derogation notice” a document separate to the policy wording that clearly states “this policy does not comply with the minimum standards because of this.....etc”. If this did not happen any claim made was considered under the relevant prescribed contract with no consideration given to the contract issued by the Insurer.

One of the detrimental changes to the Insurance Contracts Act was the removal of the requirement to provide a derogation notice in favour of providing a Product Disclosure Statement. The effects of this on the consumer will be discussed later in this document under the heading of Product Disclosure Statements.

The prescribed contracts in their current form are fair and reasonable however they were written over 30 years ago so they could do with some “modernisation” and should be reviewed. Also consideration should be given to including additional prescribed contracts particularly in relation to Strata Title and Small business including business public liability policies.

### **Product Disclosure Statements. (PDS)**

The PDS or policy wording is the document that the Insurer issues to the customer and is the basis upon which claims are settled. As mentioned previously the Insurance Contracts Act has 6 prescribed contracts or minimum standard covers, for example the Home and Contents cover.

The Home and Contents prescribed contract is less than 12 pages in length. It was decided that the average consumer struggled to read this document so legislation was introduced requiring the insurers to issue the PDS in plain English. This doubled the size of the document. It was then decided that the consumer still struggled to understand this document so summary of covers was introduced. It was still too hard so a key facts sheet was introduced.

The effect of all this is that we have gone from a relatively simple, less than 12 page document to now having 50 plus page monstrosities that even a seasoned Insurance professional struggles to comprehend. The consumer has no hope.

Over the past few years there has been an increasing trend of Insures including unreasonable and in some cases dangerous, irresponsible exclusions in their PDS's. This is even more evident now with the rise of the cheap on line insurers. The safety net provided by the Insurances Contracts Act is no longer effective because of the complexity of the PDS. The “fine print” is well and truly back in fashion.

Some of these PDS are so bad that it could be compared to selling a car without seatbelts, brakes, air bags or any other safety equipment. The Government and the General public would not allow this yet a similar thing is happening every day in the Insurance industry.

The simple solution is to reintroduce the requirement to provide a derogation notice with all PDS's.

### **Professional Advice.**

The introduction of the Financial Services Reform Act and the categorization of advice into

Personal,

General and

No Advice

has been effective in so far as improving the quality of Professional Advice across the whole industry. Thereby benefiting the consumer.

However those customers the deal with companies that are operating under a “No Advice” model have received no such benefits or protection. Again as mentioned previously the problem could be solved by reintroducing the derogation notice.

### **Financial Ombudsman Service (FOS)**

FOS is there to protect the consumer and on the whole they perform this role admirably. However recent changes particularly in relation to the “joinder provisions” and plans to create a “one stop shop” for the whole Financial Service Sector will have a detrimental effect on those consumers that choose to use a professional for their insurance requirements.

Over the last few years there has been a noticeable shift in the attitude by Insurance companies and FOS in respect of claims disputes primarily driven by two factors

- The continued reduction of talent and experience within the industry and
- The heavy involvement of the legal profession in just about everything. (Policy interpretation, IDR panels, Claims disputes, FOS submissions etc)

It is now common to see regular (almost daily) breaches of the Insurance Contracts Act.

Past disputes that the Insurance Contracts Act was introduced to curtail our now reoccurring at an alarming rate.

The recently introduced “joinder” provisions (backed dated to 01/01/2015) will perpetuate this change of attitude to the detriment of the consumer.

More and more insurers are turning the disputes process into an extension of the legal process by engaging law firms or in house legal practitioners to respond to disputes on their behalf. This places an unrepresented client at an even greater disadvantage.

In many instances the broker's expertise results in a more level playing field and without the vigorous involvement of the broker the dispute may have failed.

Any provision that may result in a broker becoming less inclined to act as an Authorised Representative of the client in a dispute or that may result in a broker effectively watching their back whilst acting as the Authorized Representative of the client in a dispute will ultimately put the client at a disadvantage.

### **How the Joinder provisions will disadvantage the client.**

An Insurer and broker working closely together to protect their own interests at the expense of the client.

Insurers providing submissions that ignore the reason of the dispute and deflect blame to the broker,

Insurers encouraging clients by direct contact with them to lodge a dispute against the broker to avoid addressing the dispute against themselves.

The disputes system turned into a legal process. The very thing it was introduced to stop in the first place.

In recent times there has been imbalance in favour of the Insurance companies. A broker acting as a representative of the client has been able to correct this imbalance. However following the introduction of the Joinder provision this ability may now be taken away, if a broker can no longer confidently and vigorously represent their client in a dispute.

A suggested solution would be that where a broker has been appointed by the client to act as their Authorised Representative in a dispute, that the broker then be excluded from the prospect of a joinder provision. In circumstances where the broker has not been appointed as Authorised Representative of the client for the purposes of a dispute, joinder provisions may be applied.

### **Affordability**

Whether you are believer in climate change or not there is no doubt that the frequency and severity of natural disasters are and will continue to increase. This will put even more pressure on the cost of insurance.

The government has conducted an enquiry into the cost of insurance and whilst the report has not been fully released or addressed the findings will have very little impact on pricing and in some cases result in increases.

Insurers may say they are reducing premiums and are keeping increases to a minimum and it may well be the case when looking at their overall premium pool. However the real issue is the how they collect the premiums that make up the pool.

With the advent of technology, mitigation initiatives and Insurers being more selective in choosing their risks the gap between what is considered a good and less desirable is increasing.

Below is a simple example of what has been happening over the last few years.

2 years ago - A house in Brisbane - \$2,000, a house in North Qld - \$3,000, premium pool collected - \$5000

Current period - a house in Brisbane - \$1000, a house in North Qld - \$4000, premium pool collected - \$5000

The insurers can confidently state the statistics show that premiums have remained stable over the last few years and in many cases have actually decreased. However a lot of people have seen 100% or more increases.

Whilst the above example is in relation to cyclone areas the same has been happening across Australia in Flood areas, bush fire areas, hail areas and high crime areas. The same widening of the gap has also been occurring within different industry types and different construction types.

Individual risks are being made to “stand on their own” which contradicts the basic principal of insurance, to spread the risk. The premium of the many pay for the claims of the few. Unless something is put in place to encourage insurers to be less selective and to spread the risk the number of individuals and even whole towns and areas of the country that cannot afford insurance will continue to increase.

The Insurance Industry has been pushing mitigation as a solution and the inquiry in to pricing in North Queensland appears to draw the same conclusion. Whilst this will have some small benefits it is not the solution. As technology and the access to information continues to improve the selective nature of insurance companies will increase and all that will be achieved is a further widening of the gap between affordability and unaffordability.

The solution to affordability is simple, spread the risk far and wide and through as many insurance companies as possible. There are many ways this can be achieved, however as the implementation could potentially be quite complex more thorough research and consultation will be required.

One thing for certain is that this issue will not correct itself without some form of Government or legislative intervention.

## **Taxes**

The four taxes that relate to insurance premiums are

GST

Stamp Duty

Emergency Services Levy

Terrorism Levy.

There are many arguments for and against the removal and/or reduction in insurance related taxes. However, irrespective of which side of the debate you support the real issue is how these taxes are collected.

The current method of a percentage of the insurance premium severely disadvantages the lower income earners and in particular the aged pensioners. Both these groups tend to live in the older houses and /or in less desirable areas. As a result of the insurance companies risks selection and pricing both these groups usually pay significantly higher insurance premiums. This is further exasperated if they were to live in a cyclone area, flood area, bush fire area or other designated higher exposure areas.

As a director of an insurance broker I have firsthand knowledge of the extreme differences in the insurance premiums. The below example is not fanciful and can be demonstrated by reference to our client records.

A married couple with no children with a new brick house in Brisbane in a designated low risk area may attract an insurance premium of \$2000.

A pensioner with an older house in a designated high risk area in Townsville may attract an insurance premium of \$10000.

Based on the current tax rates the person in Brisbane would pay \$409 whilst the person in Townsville would pay \$2045.

A fairer system that more evenly distributes the tax burden is required.

A simple solution would be to increase the base percentage and introduce a capping or maximum amount payable.

## **Conclusion**

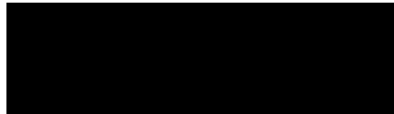
The current state of the insurance industry and the issues being addressed now are similar to the conditions that existed over 30 years ago prior to the introduction of the Insurance Contracts Act.

The Insurance Contracts Act was a very successful piece of legislation because it had a long term view and focused on fundamental reform. Recent times have seen a short term, quick fix mentality. You can give someone pain killers to help with an injury but the problem is only going to get worse until such time as the cause of the pain or injury is addressed.

It is now time to take a long term view and a good start would be to successfully address the abovementioned issues.

## **About the Author**

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33 years insurance experience (20years underwriting – 13 years insurance broking)

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## **Disclaimer**

This document is written to reflect my personal views only.

It is not written on behalf of any of the abovementioned associations. Reference to them was only included to demonstrate my involvement and experience in the Insurance Industry.