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Dear ██████████

**Submission: Northern Australia insurance Inquiry**

Thank you for the opportunity to comment on the Northern Australia Insurance Inquiry Issues Paper.

While we provide legal or financial counselling services within Victoria only, our insurance policy work has a national focus. This submission makes general comment on what are the key issues nationally, in our view:

- the impact of conflicted remuneration and information asymmetry,
- how disclosure and transparency can be improved,
- the impact of unfair contract terms laws, and
- how consumer data management can be improved.

Our comments are detailed below.

**About Consumer Action**

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

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## 2. The competitiveness of markets for insurance in northern Australia

### Commissions and countervailing power

Insurers are clearly in a superior bargaining position to their customers.<sup>1</sup> A key cause of this is the ‘information asymmetry’ between insurers and their customers. As the Senate Economics References Committee inquiry into Australia’s general insurance industry found:

*Information asymmetry that favours insurers can hinder consumer decision-making because of a lack of understanding about premium pricing, policy coverage and personal risk. This can, in turn, lead to poor consumer outcomes, such as inflated premiums, underinsurance, or coverage that is inappropriate to their needs.<sup>2</sup>*

This effect significantly inhibits competition in the domestic insurance market. It also leads to devastating ‘moments of truth’, when consumers claim on their insurance and discover that policy exclusions or conditions mean that insurers will not pay their claims.

Unfortunately, we have seen cases where insurance brokers do not represent their clients’ interests and sell unsuitable insurance that is not valuable. Clients do not have countervailing power in relation to their brokers due to the same information asymmetry issues and, in some cases, the need to use a broker to access insurance or get a ‘good deal’. As the Issues Paper states:

*Commissions and other benefits that an intermediary might receive may affect their incentives in relation to the advice they provide, and where they arrange for the consumer’s cover to be placed.<sup>3</sup>*

We agree with this assessment. In our experience, conflicted remuneration of intermediaries has driven unsuitable selling and caused serious systemic problems which have disadvantaged consumers. This is true across many consumer markets.

## 5. Regulation

### 5.1 Information, disclosure and transparency

Disclosure requirements are intended to ensure that people understand the insurance that they buy. It is clear that the primary disclosure obligation—to provide customers with a Product Disclosure Statement (PDS)<sup>4</sup>—is not fulfilling this purpose.

There is now widespread acknowledgement that this type of mandatory disclosure is an outdated consumer protection. As ASIC stated in its submission to the 2014 Financial System Inquiry:

*Economic research in behavioural economics, as well as the experience of regulating retail financial markets, indicates that investors and consumers are prone to behavioural biases that mean decision making is often not instrumentally rational. This*

<sup>1</sup> Issues Paper, page 11.

<sup>2</sup> Senate Economics References Committee, *Australia’s general insurance industry: sapping consumers of the will to compare*, August 2017, para 3.2.

<sup>3</sup> Issues paper, page 11.

<sup>4</sup> *Corporations Act 2001* (Cth) Part 7.9 Division 2.

*undermines the effectiveness of disclosure as a regulatory tool. Importantly, these behavioural biases are significant and systematic, rather than random and trivial.*<sup>5</sup>

In 2017, the Insurance Council of Australia published independent research which found that people are not relying on mandated disclosure. It reported that approximately 80% of people do not read the PDS before buying insurance.<sup>6</sup>

While product information at the point of sale is necessary, current disclosure requirements cannot be described as an effective consumer protection per se.

We strongly support the government's intention to improve disclosure, information and transparency for consumers. In particular, the slated Treasury review of certain proposals of the Senate Economics References Committee could lead to changes which will have a significant impact for consumers. These include:

- mandating that insurance renewal notices must include the prior year premium and component pricing,
- setting standard definitions for key terms in insurance contracts,
- reviewing the standard cover regime, in particular, the efficacy of the disclosure requirements, and
- improving consumer comprehension of Key Fact Sheets.<sup>7</sup>

In our view, changes to disclosure laws should be based in an understanding of behavioural economics and aimed at improving consumers' understanding of products and ability to choose products which are suitable for them.

Industry also has a significant role in making disclosure work for consumers. The Insurance Council of Australia (ICA) is currently consulting in the review of its General Insurance Code of Practice. The ICA has devised a draft set of best practice disclosure principles.<sup>8</sup> We believe that industry can play an immediate part in improving consumer comprehension and choice by focusing on the effectiveness of disclosure, over and above compliance with the existing legal requirements.

Technology is increasingly being used by insurers to hone their own marketing, underwriting and claims assessment processes. The industry should also harness the potential of data and technology to provide consumers with more suitable products. Some examples may include:

- requiring online customers to answer 'knock out' or filter questions to assess whether they can claim on a policy, and whether it covers what they are most likely to claim for,
- asking comprehension questions to ensure that customers understand the key features of a policy before they purchase,

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<sup>5</sup> ASIC, *Financial System Inquiry: Submission by the Australian Securities and Investments Commission*, April 2014, para 40.

<sup>6</sup> Insurance Council of Australia, *Consumer Research on General Insurance Product Disclosures: Research findings report*, February 2017, page 18.

<sup>7</sup> *Australian Government response to the Senate Economics References Committee report: Australia's general insurance industry: sapping consumers of the will to compare*, December 2017.

<sup>8</sup> Insurance Council of Australia, *Interim Report: Review of the General Insurance Code of Practice*, November 2017, Proposal 2.

- providing user-friendly tools such as sum insured calculators and risk information (for example, the NRMA Safer Homes), to assist people to understand their own risk profile, mitigation options and insurance needs, and
- using non-text and accessible information to ensure that people with a range of English and comprehension levels can find out what a policy covers.

There are no doubt many other options open to insurers right now to ensure that more customers are buying suitable insurance products.

## 5.2 Unfair contract terms

While affordability and availability of insurance are obviously critical, so too is the suitability and fairness of insurance. While insurers continue to enjoy an exemption from unfair contract term laws, there is no consumer protection which effectively assures consumers that their insurance policy will be suitable or 'fair'. There is no advantage to consumers of the insurers' exemption continuing, and we strongly support the government's intention to remove the exemption.<sup>9</sup>

For as long as the industry does not have to ensure that their contract terms protect their legitimate business interests and are clear and transparent, there is ambiguity in why a policy includes particular conditions and exemptions, and how the premium is calculated. Good price does not necessarily translate to good value. There are currently few incentives for insurers to offer good-value and fair policies which provide appropriate cover.

It is clear that insurers should be required to ensure that their contracts meet the same basic commercial standards of fairness as other financial products.

Fairer contracts would benefit consumers and insurers by:

- preventing disputes about unexpected and unfair claims outcomes,
- increasing consumer trust and confidence in the insurance industry,
- levelling the playing field between insurers, so that cheap, poor-value and unsuitable products do not prevail, and
- providing for more efficient regulation of insurance, by aligning it with the regulation of other consumer contracts.

## 5.3 Data availability and use

The age of big data means insurers can glean very detailed pictures of the customers and potential customers. UK research has shown that the trust in institutions to use data appropriately is relatively lower than the trust in those institutions generally.<sup>10</sup> This 'data trust deficit' is likely to also exist in Australia and is an indicator that effective data management regulation is important.

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<sup>9</sup> Kelly O'Dwyer MP, Media Release, Government responds to Northern Australia Insurance Premium Taskforce and General Insurance Senate Inquiry, 18 December 2017, available at: <http://kmo.ministers.treasury.gov.au/media-release/120-2017/>.

<sup>10</sup> Royal Statistical Society, Research on trust in data and attitudes toward data use / data sharing, October 2014, available at: <http://www.statslife.org.uk/images/pdf/rss-data-trust-data-sharing-attitudesresearch-note.pdf>.

As customer data becomes more widely used by insurers, including in marketing, underwriting and claims assessment, the regulation of how insurers manage this data is becoming outdated. We support the Government's announcement of a forthcoming Consumer Data Right, to give people ownership of their own data which companies hold.<sup>11</sup> It does not appear that this right will apply to insurers immediately, but we urge Governments to extend it. Consumers could use customer data in buying insurance, for example, to quickly and easily generate quotes and shop around.

However, we remain concerned with two issues which big data give rise to:

1. data privacy, in particular, third-party disclosure, and
2. discrimination on the basis of data.

### ***Third-party disclosure***

In accordance with the *Privacy Act 1988* (Cth), insurers' privacy policies set out which third parties the insurers will disclose information to, and why. These are the standard terms on which people deal with insurers, including when they take out a policy.<sup>12</sup>

There is inconsistency in how insurers inform people about their privacy policies. Some insurers include privacy and third-party disclosure information in their PDSs.<sup>13</sup> At least one policy that we reviewed did not mention privacy at all.<sup>14</sup> One insurers' PDS gives the insurer broad remit to:

‘disclose your personal information to *others with whom we have business arrangements* for the purposes listed in the paragraph above or to enable them to offer their products and services to you’.<sup>15</sup>

Considering that very few people look at the PDS when they buy insurance,<sup>16</sup> we expect that even fewer look at the privacy policy. Consumers are therefore very unlikely to know how their information may be shared. This is the primary barrier to consumers enforcing their own data privacy rights. Whether or not they can control it is an important secondary issue.

### ***Discrimination***

Discrimination on the basis of individual risk, with appropriate data, can be legitimate in some circumstances. However, insurance is by nature a form of ‘pooled risk’, combining higher and lower risk customers. This is the critical consideration in how insurers use the increasing

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<sup>11</sup> Angus Taylor MP, Media Release, Australians to own their own banking, energy, phone and internet data, 26 November 2017, available at: <https://ministers.pmc.gov.au/taylor/2017/australians-own-their-own-banking-energy-phone-and-internet-data>.

<sup>12</sup> The General Insurance Code of Practice reiterates insurers' commitment to comply with the principles under the Privacy Act, but does not provide any additional consumer rights or protections.

<sup>13</sup> For example: QBE, *Home Cover: Insurance Product Disclosure Statement and Policy Wording*, date effective: 27 November 2010; RACV, *Home Insurance Product Disclosure Statement and Policy Booklet*, prepared 3 March 2017.

<sup>14</sup> AAMI, *Home Building Insurance: Product Disclosure Statement*, dated 1 October 2013.

<sup>15</sup> Allianz, *Home Insurance Product Disclosure Statement*, prepared on 31 March 2015.

<sup>16</sup> Research commissioned by the Insurance Council of Australia found only 22% of people used the PDS before they purchased home and contents insurance, and only 4-5% used it as their main source of information: Insurance Council of Australia, *Consumer Research on General Insurance Product Disclosures: Research findings report*, February 2017, p 18.

individual data available to them. Certain types of insurance, such as home and contents, are basically an essential service. Access to these types of insurance is a necessity for people of many different risk profiles.

As insurers become more able to understand people's individual risk profiles, there is a significant risk that more 'uninsurable' groups of people will start to emerge. This has obviously been the case with building insurance in parts of northern Australia, but it may increasingly become the case in other areas and with other types of insurance. There will be more people who insurers deem too high risk and will not insure, or will not insure at an affordable cost.

This is a particular concern where there is a lack of transparency not only of the data insurers rely on, but the algorithms and analysis used to make decision on the basis of that data. The complex use of data will have real impacts on people's lives, and insurers must be open about how they are using data, and how this complies with the law, including discrimination laws.

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

Yours sincerely,

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