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2 February 2017

By email

Gavin Jones
Director
Merger and Authorisation Review
Australian Competition and Consumer Commission

Dear Gavin

Aioi Nissay Dowa Insurance Company Australia Pty Ltd & Ors – applications for authorisation A91556 – A91557

We refer to your letter dated 21 December 2016 setting out the ACCC's preliminary views about the proposed conduct. We appreciate the opportunity to respond to the ACCC's concerns and to provide further information about the proposed conduct.

1 Addressing a market failure

The applicants consider that high commissions paid in the motor vehicle dealership channel contribute significantly to the market failure identified by ASIC by providing incentives to engage in the inappropriate sales practices identified in the recent ASIC reports into that channel, such as providing incomplete information or explanation of the products, pressuring or rushing customers, downplaying the cost of products, using pre-filled application forms, and in some cases misrepresenting the value or necessity of add-on insurance products.

These sales practices can prevent customers from making informed decisions about the products they are being offered, including the value of those products and the alternatives available elsewhere. In reducing the level of commissions paid in the motor vehicle dealership channel, the applicants intend and expect to alter these incentives and minimise these sales practices, directly addressing the market failure.

1.1 Commissions and the market context

In its letter to the applicants, the ACCC describes the central issue as one of "lack of transparency" where "many consumers are not put in a position to make rational, well-informed choices when buying add-on insurance products through motor vehicle dealerships". The applicants consider that this description is consistent with the market failure identified by ASIC.

ASIC and the ACCC have both acknowledged the significant contribution of high commissions to a sales context that reduces customers' ability to make informed decisions when purchasing insurance products. For example, ASIC's submission to the Financial System Inquiry notes that:

For many years, the market for consumer credit insurance was characterised by problems of mis-selling of policies that included significant exclusions that limited their usefulness. The selling of such policies was driven by large commission payments for brokers.¹

The ACCC reached a similar conclusion in its earlier Consumer Credit Insurance Review:

[I]t appears that representations are being made that the purchase of CCI policies is mandatory in certain circumstances in order to be granted a loan and therefore to be able to purchase a product (e.g. motor vehicle or other consumer durable). This is sometimes taken one step further by including the cost of the policy in the amount borrowed and completing the insurance form without consulting the consumer.

It appears that some sellers of CCI have engaged in this conduct partly due to incentives arising from high commissions and partly due to inadequate training.²

The applicants have proposed a 20% cap on commissions applying to all add-on insurance products sold through the motor vehicle dealership channel in order to reduce the incentives to engage in practices that may contribute to market failure.

In its letter, the ACCC accepts that the cap on commissions is likely to reduce the risk of problematic sales practices “to some extent”, but argues that a 20% commission “would still provide strong incentives for dealers to maximise sales of insurance”. The applicants acknowledge that any commission provides incentives to maximise sales, but they consider that a reduction from up to 79% commission to 20% commission applying consistently to all products sold at point of sale through the motor vehicle dealership channel, and to all benefits in the nature of a commission including marketing subsidies and other volume-based payments, will significantly affect incentives and substantially reduce the risk of problematic sales practices.

1.2 Complementary measures

The applicants acknowledge that the reduction in commissions will not achieve this result by itself, and they are also developing a range of other measures to address or counter these practices, reduce information asymmetries and help customers make better-informed decisions. These measures include increased training and monitoring and improvements to the accuracy, relevance and effectiveness of customer information before, at and after the point of sale, in particular:

- **Customer information and systems validation:** where applicable, insurers will implement systems to collect customer information that will identify and prevent the sale of insurance to consumers who would not on the basis of that information be eligible to make a claim, or would receive limited value from the product. General insurers have also committed, on a prospective basis, to refunds for consumers who buy policies they were unable to substantially benefit from at the time of purchase.
- **Training and monitoring:** insurers will review and strengthen dealership training on compliance and systems to ensure that appropriate conduct is clearly defined, and monitoring obligations will be clarified.

¹ ASIC, “Financial System Inquiry interim report: Submission by the Australian Securities and Investments Commission”, August 2014.

² ACCC, “Consumer Credit Review: Final Report”, July 1998 at p 27.

- **Product disclosure:** the general insurance industry is in the process of developing and consumer testing point of sale product information to better assist consumers to assess the value of products against their needs and circumstances. Life insurers will review the results of this process and introduce similar disclosure documents as appropriate.
- **Sales practices:** general insurers will commission independent reviews of insurer compliance and risk management procedures, and the ICA's "Understand Insurance" website will enhance understanding about the range of general insurance products that could be offered through motor dealers.
- **Post-sale engagement:** following a purchase, insurers will contact customers to ensure they are aware of the product they have purchased and their cooling-off rights, and will implement annual reminders in the case of multi-year products.
- **Single premiums:** insurers that offer a single loan-financed premium will also offer a non-financed option, which may include cash payment and payment by instalments; customers will be given clear information about payment options and their implications.
- **Product design:** general insurers will review their policy inclusions and exclusions with a view to increasing product coverage where possible for the benefit of consumers, and life insurers will review products to ensure they are sustainable, affordable and suitable to customers.

All of these measures can be agreed through individual or industry negotiation with ASIC as they either do not require collective action or do not involve any risk of breaching the competition law if approached collectively.

The process for ensuring that these and other measures considered necessary to address product design and sales practice issues is being managed by ASIC. ASIC has been communicating closely with the applicants on those matters for some time and has made clear its expectations. Most recently, ASIC has arranged a series of working group meetings to be attended by the applicants and consumer groups in January and February 2017 to conclude their requirements. A copy of the draft Terms of Reference prepared by ASIC in relation to the meetings has been included as Attachment B. As stated in that document, ASIC intends to issue a set of principles, based on the output of the working group meetings and require insurers to finalise their measures in accordance with those principles.

However, these measures will not be effective without also addressing the contribution that high levels of commission make to the market failure that ASIC has identified.

In this the applicants disagree with the ACCC's assumption that "the success or otherwise of these measures is not related to any cap on commissions". The applicants consider that the success of these measures depends to a considerable degree on reducing the incentives to mis-sell insurance products that would significantly undermine the impact of measures.

These incentives cannot be addressed by insurers on an individual basis, since any insurer who reduces commissions will quickly lose its access to distribution in this channel to insurers that continue to pay high commissions. They can only be addressed through the authorisation process.

This is precisely the kind of difficulty that has been identified by ASIC:

There are issues or practices that exist today that cause consumer detriment, and that most if not all stakeholders recognise as problematic. Nevertheless, because of the inherent difficulties of collective action, even those in industry who would like to see the practice end, cannot act—the ‘first mover’ disadvantage of doing so would be too great and competition laws may be a barrier to industry acting collectively in some cases.³

The conduct for which authorisation is sought is an integral part of a broader approach to address the market failure identified by ASIC and is the only part of that approach that requires ACCC authorisation.

1.3 Alternative measures

The applicants acknowledge that submissions have suggested additional or alternative measures to address the market failure identified by ASIC. In particular, the Consumer Action Law Centre (**CALC**) suggests that there could be a mandatory delay between the sale of the primary product and the sale of the add-on product. ASIC has also raised such a measure as a potential remedy to address its concerns, though substantive discussions have not yet been had with industry on that option. We note that CALC will be attending the upcoming ASIC working group meetings (referred to above) and expect discussions to occur in that forum.

2 Reducing prices and increasing value

The applicants acknowledge the concern that a reduction in commissions will not by itself lead to a reduction in prices by insurers, and could result in a transfer of value from dealers to insurers.

The applicants have proposed the 20% cap with the expectation and intention of reducing prices and increasing value for consumers. They understand, however, that there needs to be a mechanism in place to ensure that that occurs in practice. To that end, they are putting in place a reporting mechanism that will ensure that ASIC can monitor both prices and loss ratios with the expectation that value will be transferred to consumers rather than insurers and the ability to take further action against individual insurers who do not meet that expectation. That mechanism is discussed further below.

2.1 Data reporting to ASIC

The applicants have engaged Finity Consulting (**Finity**) and Insurance Statistics Australia (**ISA**) to assist in the implementation and execution of a system of regular reporting of detailed information of premiums and loss ratios to ASIC.

This information will allow ASIC to compare the price and value of add-on insurance products before and after the introduction of the cap on commissions and on an ongoing basis. ASIC have made it clear that they will actively monitor premiums and loss ratios to ensure that all insurers are taking advantage of the opportunities for greater value presented by the reduction in commissions, and will take any action it considers necessary if they are not.

These actions may be directed towards individual insurers and may range from adverse publicity to new licence conditions or action under consumer protection laws; or they may be directed towards the entire industry through class orders or other regulations. Reporting to ASIC will give insurers very

³ ASIC, “Financial System Inquiry interim report: Submission by the Australian Securities and Investments Commission”, August 2014.

strong incentives to reduce their prices and increase their loss ratios in order to avoid these consequences.

ISA have met with the insurers who sell add-on insurance through the motor vehicle dealership channel and developed a detailed data specification that insurers have agreed to provide on a quarterly basis in relation to all add-on insurance products sold through the dealership channel. The draft specification includes:

- details of the products and options offered by the insurer within the broader categories of comprehensive insurance, purchase price protection insurance, personal and unregulated consumer credit insurance, tyre and rim insurance, mechanical breakdown insurance, and gap insurance;
- details of the representatives authorised to deal in each of these products, including circumstances in which they are instructed not to sell policies and the number of representatives who have had authorisations cancelled or have been warned in writing for misconduct or have had commissions clawed back in relation to each of these products;
- the pricing of each product and cover option, including details of any variable pricing and the minimum and maximum levels within which prices can be varied;
- details of all policies issued including the issuer's company code, the product code, the channel, the name of the authorised representative, the coverage, the policy number, the start and end dates, the premium and commission, the policy status, the cancellation and effective expiry dates, any amounts refunded, the gross and net loan amounts (for gap and CCI policies), the sum insured (for CCI policies), maximum shortfall and additional benefits amounts (for gap policies), and the age and employment status of the policyholder at commencement;
- details of all claims made including the issuer's company code, the claim number, policy number and product code, the date of the report, the type and specifics of the claim, the amounts paid in the relevant quarter and to date, the amounts paid to meet shortfall and for additional benefits (for gap policies), the internal management cost and assessment cost if available, the estimate of future payments, the age and gender of the claimant, the claim status and the reasons for any denial.

ISA will continue to refine this data specification with insurers and with ASIC to ensure that data will be reliably collected, consistently reported and provided in a format that can be interrogated by ASIC and provides a clear view of the price and value of add-on insurance products over time.

2.2 Target loss or claims ratios

The applicants note calls from CALC to establish target claims ratios. The applicants note that in some states of the United States, life insurers are required to meet a minimum return in claims, and regulations prescribe a formula for premiums that will be presumed to comply with the minimum.⁴ These loss ratios refer to products that are significantly more homogeneous than those offered in Australia, and require state regulators to assess whether rates that differ from the *prima facie* rates can reasonably be expected to result in the target loss ratios – effectively setting prices by regulation.

⁴ ASIC Report 471, *The Sale of Life Insurance through Car Dealers: Taking Consumers for a Ride*, February 2016 at p 32; *Insurance Regulation 9 (Consumer Credit Insurance)*, issued by the Division of Insurance in the Department of Business Regulation of the State of Rhode Island and Providence Plantations.

Minimum or target loss ratios become more difficult to meaningfully define or measure when multiple heterogeneous products are involved and prices are set by the market rather than through regulation or regulatory approval. These measures are also unlikely to take into account changing market conditions that may significantly affect loss ratios outside the control of insurers, particularly where products remain in place for many years.

As the Trade Practices Commission has noted:

There is some doubt about whether the system operating in the US is effective in meeting its objective. Loss ratio figures in the US available to the Commission are lower than the benchmarks. They are higher than in Australia but other differences between the CCI markets of the two countries may account for the difference.

Determination of an appropriate ratio, or range of ratios, would not be straightforward. There is also the question of whether there should be different ratios for the different classes of CCI to prevent one class from subsidising another. There is considerable debate over the setting of ratios in the US.⁵

Setting loss ratios appropriate to the diverse range of products and product classes sold through the motor vehicle dealership channel and contemplated by this proposal would significantly compound these difficulties. Target loss ratios would also present particular problems for new entrants who may not be able to fully fund their operational costs while meeting those targets.

3 Enforcement mechanism

The applicants acknowledge concerns raised by CALC that the proposal set out in the application does not contain a full monitoring and enforcement framework. The applicants have been developing the monitoring and enforcement framework as the application has proceeded in order to introduce the cap on commissions as quickly as possible.

3.1 Code monitoring and enforcement

The applicants are continuing to develop a code of conduct around the cap on commissions and reporting to ASIC. The proposed Commission Code of Conduct would replicate the monitoring and enforcement framework of the General Insurance Code of Practice (**GI Code**), while adding a further sanction that mirrors section 145 of the National Credit Code in requiring an insurer to pay to the insured the whole amount or value of any commission paid in breach of the cap on commissions.

The insurers would propose to establish or engage a new compliance entity with a role similar to the Code Governance Committee (**CGC**) responsible for the GI Code, which currently delegates to the Financial Ombudsman Service Code Compliance and Monitoring Team (**FOS Code**). Under this approach, the insurers would conduct a tender process for the compliance role, inviting tenders from appropriate bodies and firms who have relevant experience. The insurers expect the major accounting firms to have the requisite skillset and appetite to take on such a compliance role.

An update to the Proposal initially attached with the application, in the form of a proposed Commission Code complete with monitoring and enforcement provisions, is set out in Attachment A.

⁵ TPC, *The Market for Consumer Credit Insurance*, 30 June 1991 at p 66.

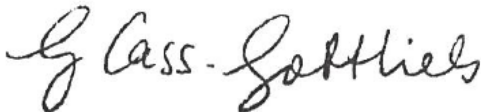
4 Conclusion

The applicants consider that a 20% cap on commissions directly addresses the market failure identified by ASIC by reducing the incentives for dealers to engage in sales practices that result in poor consumer outcomes. The applicants acknowledge that the reduction in commissions is only one part of a suite of measures that will achieve this result. Other complementary measures being explored by ASIC (in consultation with the industry and consumer groups) will also address the identified market failure and together, the applicants consider that sales practices will improve, information asymmetry will be remedied and consumers will ultimately benefit.

However, the applicants consider that the complementary measures being developed cannot alone address the market failure identified by ASIC. ASIC agrees with this analysis.

Absent a cap on commissions, the applicants are of the view that commissions will remain at high levels and prices will not fall. The applicants therefore consider that the conduct subject to authorisation would provide net public benefits that would not otherwise be achieved, and accordingly that authorisation should be granted.

Yours sincerely

A handwritten signature in black ink that reads 'Gina Cass-Gottlieb'.

Gina Cass-Gottlieb

Partner

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Attachment A
Add-on Insurance Reform
Commission Code

1 Introduction

- 1.1 Customers may be offered a range of insurance products that help protect against risks to their motor vehicle or to their ability to repay a loan associated with the purchase of a vehicle. These “add-on insurance” products can provide convenience, certainty and peace of mind to customers. However, there are concerns that some add-on insurance products do not always represent value for money due in part to the level of commissions paid to the motor vehicle dealership channel, which may increase prices and encourage inappropriate sales practices.
- 1.2 General and life insurance providers are developing a range of measures to address these concerns. This Code will complement those measures but is specifically aimed at addressing the value of add-on insurance products by limiting the commissions paid in respect of these products, which will flow through to reduced premiums, and providing for comprehensive data reporting to ensure accountability for improvement in the value of these products.

2 Objectives

- 2.1 The objectives of this Code are:
- (a) to increase the value of add-on insurance products sold through the motor vehicle dealership channel;
 - (b) to reduce incentives to mis-sell add-on insurance products;
 - (c) to prevent circumvention of the limit on commissions;
 - (d) to allow monitoring of movements in prices and loss ratios.

3 Definitions

In this Code:

“**ADI**” means an authorised deposit-taking institution authorised under the *Banking Act 1959*;

“**add-on insurance**” means all general and life insurance products issued or arranged:

- (a) by a **motor vehicle dealership**, an **associated credit provider**, an **associated broker** or an **independent finance broker**, or by any of their agents; and
- (b) in connection with a **motor vehicle** or a loan associated with the purchase of a **motor vehicle**,

but does not include compulsory third party insurance, or commercial motor insurance issued to a **motor vehicle dealership** to cover risks to the inventory of the **motor vehicle dealership**;

“**associated broker**” means any broker, adviser or other person or entity who issues or arranges insurance products pursuant to:

- (a) a contract, arrangement or understanding with a **motor vehicle dealership**, an **associated credit provider** or an **independent finance broker**; or
- (b) a referral from a **motor vehicle dealership**, **associated credit provider** or **independent finance broker**,

and includes a prospective **associated broker**;

“**associated credit provider**” means a person that provides credit in connection with the financing of a **motor vehicle** pursuant to:

- (a) a contract, arrangement or understanding with a **motor vehicle dealership**; or
- (b) a referral from a **motor vehicle dealership**;

and includes a prospective **associated credit provider**;

“**commission**” includes:

- (a) any financial or other benefit in the nature of a commission; and
- (b) any form of monetary consideration or any form of non-monetary consideration to which a monetary value can be assigned;

“**data reporting entity**” means an entity nominated by the insurers and notified to ASIC from time to time to report data under clause 5 of this Code;

“**data reporting period**” means, in each year:

- (a) 1 January to 30 June; and
- (b) 1 July to 31 December;

“**FOS**” means the Financial Ombudsman Service;

“**governance entity**” means the governance entity as explained in section 7;

“**independent finance broker**” means a person that provides or arranges credit in connection with the financing of a **motor vehicle** purchased from a **motor vehicle dealership** but is not an **associated credit provider** or an **ADI**, and includes a prospective **independent finance broker**;

“**insurer reporting period**” means, in each year and in respect of each insurer:

- (a) the three-month period commencing on the date on which the insurer's financial year begins; and
- (b) each subsequent three-month period;

“motor vehicle” means a road vehicle driven by a motor, and includes a passenger car, utility vehicle, van, truck or motorcycle;

“motor vehicle dealership” means any person or entity that:

- (a) carries on the business of dealing in motor vehicles as a retailer or wholesaler; or
- (b) is an associated entity, as that term is defined under the *Corporations Act 2001*, of a **motor vehicle dealership**;

“significant breach” means a breach that is determined to be significant by reference to:

- (a) the number and frequency of similar previous breaches;
- (b) the impact of the breach or likely breach on our ability to provide our services;
- (c) the extent to which the breach or likely breach indicates that our arrangements to ensure compliance with Code obligations is inadequate;
- (d) the actual or potential financial loss caused by the breach; and
- (e) the duration of the breach;

“transition date” means the date three months after the ACCC grants final authorisation to this proposal; and

“transition period” means the period that began on 7 September 2016 and ends on the transition date.

4 Cap on commissions for add-on insurance products

- (1) This section applies to **commission** paid to a **motor vehicle dealership**, an **associated credit provider**, an **associated broker**, an **independent finance broker**, or any of their agents, in connection with an **add-on insurance product** on or after the **transition date**.
- (2) The total of any such **commission** accepted by all or any of the following—
 - (a) a **motor vehicle dealership**;
 - (b) an **associated credit provider**;
 - (c) an **associated broker**;
 - (d) an **independent finance broker**; and

- (e) any agent of a **motor vehicle dealership, associated credit provider, associated broker or independent finance broker**;

must not exceed, in amount or value, 20% of the premium (excluding government charges).

- (3) A **motor vehicle dealership, associated credit provider, associated broker, independent finance broker** or any such agent must not accept, and an insurer must not pay, a **commission** exceeding, in amount or value, the maximum allowed under this section on or after the **transition date**.

5 Transition

- (1) Any up-front payment or sign-on fee paid by an insurer in connection with an **add-on insurance** product under arrangements entered into, renewed or varied during the **transition period** must be recovered by the insurer within 30 days of the **transition date**.
- (2) Where any new, renewed or varied arrangement increases **commissions** above the level that applied immediately before the **transition period**, all **commissions** paid in connection with **add-on insurance** products under any such arrangement that exceed 20% of premiums (excluding government charges) must be recovered by the insurer within 30 days of the **transition date**.
- (3) For the avoidance of doubt:
 - (a) where an insurer can demonstrate that the key elements of an arrangement had been agreed before the **transition period**, that arrangement is not an arrangement entered into, renewed or varied during the **transition period** notwithstanding that the arrangement had not been formalised before the **transition period**; and
 - (b) any payment or benefit in the nature of an upfront payment or sign-on fee will be considered to be an upfront payment or sign-on fee, whether it is described as such or as a marketing fee, periodic payment, volume bonus or other description.

6 Data reporting

- (1) Within 30 days of the end of each **insurer reporting period**, each insurer will provide data to the nominated **data reporting entity** relating to add-on insurance products that fall into or are similar in nature to the following categories:
 - (a) consumer credit insurance, separately where issued for:
 - (i) personal or consumer use; and
 - (ii) business use;
 - (b) gap insurance;
 - (c) warranty or mechanical breakdown insurance;
 - (d) tyre and rim insurance;

- (e) loan termination or walkaway insurance;
 - (f) guaranteed buyback insurance;
 - (g) trauma insurance (if provided separately to consumer credit insurance).
- (2) Each insurer will provide details of the name and product category of each product and will separately provide the following data in relation to policies incepted:
- (a) in the three months before; and
 - (b) after,
- the **transition date**:
- (c) details of pricing (including details of government charges);
 - (d) number of policies in force;
 - (e) number of new policies issued;
 - (f) average age of policies;
 - (g) cancellation rate;
 - (h) product split;
 - (i) net earned premiums;
 - (j) gross written premiums;
 - (k) incurred losses; and
 - (l) number of claims paid,
- in respect of each product within each product category.
- (3) The nominated **data reporting entity** will provide data received from each insurer during each **data reporting period** to ASIC within 30 days of the end of each **data reporting period**.

Data reporting is intended to provide transparency and accountability and to allow ASIC to monitor the effect of the package of changes that have been proposed. The exact process and the form of data to be provided will be finalised in conjunction with ASIC and any nominated data reporting entity.

7 Code Governance

- 7.1 The **governance entity** is the independent body responsible for monitoring and enforcing compliance with this Code.

- 7.2 The **governance entity** is responsible for monitoring and enforcing our compliance with this Code, in accordance with section 8 of this Code.
- 7.3 The **governance entity** is responsible for providing quarterly reports to insurers, with recommendations on any Code improvements, Code-related issues and matters of importance.
- 7.4 The **governance entity** may outsource to an appropriate service provider any of the responsibilities of the **governance entity** set out in sections 8.6 to 8.8 of this Code.
- 7.5 Insurers are responsible for commissioning formal independent reviews of this Code from time to time. The **governance entity** may recommend to insurers that this Code be reviewed, if the **governance entity** believes the application of this Code is not meeting the objectives outlined in section 2 of this Code.
- 7.6 In addition to formal independent reviews of this Code, insurers will consult with the **governance entity**, FOS, consumer and industry representatives, relevant regulators and other stakeholders to develop this Code on an ongoing basis.

8 Monitoring, Enforcement and Sanctions

- 8.1 Any insurer, consumer or regulator or FOS may report alleged breaches of this Code to the **governance entity**.

Insurers' Responsibility

- 8.2 Each insurer will:
- (a) have appropriate systems and processes in place to enable the **governance entity** to monitor compliance with this Code;
 - (b) prepare an annual return to the **governance entity** on its compliance with this Code; and
 - (c) have a governance process in place to report on its compliance with this Code to its Board of Directors or executive management.
- 8.3 If an insurer identifies a **significant breach** of this Code, it will report it to the **governance entity** within ten business days.
- 8.4 Each insurer will cooperate with the **governance entity** in its:
- (a) review of that insurer's compliance with this Code; and
 - (b) investigations of any alleged Code breach.
- 8.5 Insurers will apply corrective measures within set timeframes, as agreed with the **governance entity**, in response to a Code breach.

Governance Entity Responsibility

- 8.6 The **governance entity** is responsible for monitoring and enforcing compliance with this Code.

- 8.7 The **governance entity** will prepare annual public reports containing aggregate industry data and consolidated analysis on Code compliance.
- 8.8 The **governance entity** will:
- (a) receive allegations about breaches of this Code;
 - (b) investigate alleged breaches at its discretion in accordance with this Code;
 - (c) provide an opportunity for insurers to respond to alleged breaches;
 - (d) determine whether a breach has occurred;
 - (e) agree with insurers any corrective measure(s) to be implemented by insurers and the relevant timeframe(s); and
 - (f) monitor the implementation of any corrective measures by insurers and determine if they have been implemented within the agreed timeframe.
- 8.9 The **governance entity** may provide any recommendations on Code improvements as a response to its monitoring and enforcement, in its quarterly reports to insurers.

Sanctions

- 8.10 If the **governance entity** considers an insurer has failed to correct a Code breach, it will:
- (a) notify the insurer's Chief Executive Officer in writing; and
 - (b) provide an opportunity for the insurer to respond within 15 business days.
- 8.11 The **governance entity** will consider any response by an insurer before making a final determination and imposing any sanctions.
- 8.12 The **governance entity** will notify an insurer's Chief Executive Officer in writing of its decision regarding any failure to correct a Code breach and any sanctions to be imposed.
- 8.13 When determining any sanctions to be imposed, the **governance entity** will consider:
- (a) the principles and objectives of this Code;
 - (b) the appropriateness of the sanction; and
 - (c) whether the breach is a **significant breach**.
- 8.14 The **governance entity** may impose one or more of the following sanctions:
- (a) a requirement that the insurer pay to the insured the whole amount or value of the **commission** paid by the insurer;
 - (b) a requirement that particular rectification steps be taken by an insurer within a specified timeframe;

- (c) a requirement that a compliance audit be undertaken;
- (d) corrective advertising; and/or
- (e) publication of an insurer's non-compliance.

8.15 The **governance entity's** decisions are binding on insurers.

Attachment B



ASIC

Australian Securities & Investments Commission

TERMS OF REFERENCE: ASIC ADD-ON INSURANCE WORKING GROUP

Revised: As of 24 January 2017

Purpose:

1. ASIC has identified a broad range of concerns in relation to the design, cover and value provided by add-on insurance products offered through car dealers, as well as with the add-on sales process itself. These are set out in our three recent reports:
 - a. *Buying add-on insurance in car yards: Why it can be hard to say no* (REP 470);
 - b. *The sale of life insurance through car dealers: Taking consumers for a ride* (REP 471); and
 - c. *A market that is failing consumers: The sale of add-on insurance through car dealers* (REP 492).
2. ASIC notes that:
 - a. Individual licensees are developing responses to the concerns identified in these reports; and
 - b. The ICA has coordinated a series of proposals (the non-price related initiatives) to respond to ASIC's concerns, set out in the letter to ASIC dated 2 August 2016.
3. While ASIC welcomes these initiatives, we consider that there is a risk that the work underway will result in inconsistent approaches across industry and will not deliver change that is comprehensive and in line with ASIC's expectations in respect of improved consumer outcomes.
4. The working group is intended to allow for more in depth discussion of the issues identified and to articulate further the regulatory expectations around consumer outcomes. The output from the working group will then be used to meet ASIC's key objective: to drive change that is in line with ASIC's expectations.
5. The group will primarily focus on the following findings in REP 492:
 - a. Finding 4: Poor product design;
 - b. Finding 6: Sales processes inhibit good decision making (also covers distribution).

Scope and Membership:

6. The working group will cover six add-on insurance products sold through the car dealer channel: GAP, purchase price protection, CCI, walkaway, tyre and rim and mechanical breakdown insurance (noting that not all insurers offer every product). The working group findings are also likely to be relevant to other products not discussed in the working group.
7. The Working Group will be chaired and hosted by ASIC. Other members of the working group will be representatives from:
 - a. the Insurance Council of Australia;

- b. the insurers active in this market, including, but not limited to, those subject to the findings of *Reports 470, 471 and 492*;
 - c. underwriting agents where they are responsible for product design and sales; and
 - d. representatives from Consumer Action Law Centre (CALC), Financial Rights Legal Centre (FRLC), Legal Aid New South Wales and Adjunct Professor Denis Nelthorpe.
8. Representatives from the Australian Automotive Dealers Association (AADA) and a small number of dealer members will attend the working group, to enable dealers to get a detailed understanding of concerns raised and ASIC's expectations, and contribute to the discussions on how issues should be addressed. ASIC may facilitate further discussion with dealers and their representatives and interested working group members after conclusion of the working group meetings.
9. Representatives from the Financial Services Council will be invited, should they wish to attend.

Process and outputs from the Working Group

10. ASIC will introduce each meeting by setting out its concerns with the design, distribution and sale of add-ons through the car dealer channel in a paper for the working group, and the issues will be illustrated by examples. These will not be attributed to an individual insurer/underwriting agent, but reflect common approaches observed by ASIC during its investigations.
11. ASIC will also set out its expectations for how these issues should be addressed to deliver better consumer outcomes. These will be expressed at a level of principle, so as to allow for a degree of flexibility in how licensees achieve the improved outcomes.
12. Industry and consumer groups will be invited to discuss and challenge both issues and expectations (for example, discussing claims experiences in relation to a particular product, or contributing specific examples from work with consumers). The use of non-attributed examples is intended to encourage insurers/underwriting agents to be able to engage freely at a level of principle.
13. Following completion of the working group discussions, ASIC will produce a refined set of issues and principles.
14. Based on these outputs, ASIC will write to:
- a. Individual licensees asking them to report back to ASIC within 4-6 months on how they have addressed these issues (to the extent they are relevant to them) in line with the high level principles;
 - b. The ICA, setting out any areas where the ICA's work programme should go further to ensure ASIC's concerns are fully addressed.
15. It is expected that the summary of issues and principles will also assist the independent reviewer carrying out the review of the ICA's Code of Practice scheduled for 2017.