



Law Council
OF AUSTRALIA

Legal Practice Section

Policy Questions arising from Module 6

**Royal Commission into Misconduct in the Banking, Superannuation and
Financial Services Industry**

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About the Law Council of Australia

The Law Council of Australia exists to represent the legal profession at the national level, to speak on behalf of its Constituent Bodies on national issues, and to promote the administration of justice, access to justice and general improvement of the law.

The Law Council advises governments, courts and federal agencies on ways in which the law and the justice system can be improved for the benefit of the community. The Law Council also represents the Australian legal profession overseas, and maintains close relationships with legal professional bodies throughout the world.

The Law Council was established in 1933, and represents 16 Australian State and Territory law societies and bar associations and the Law Firms Australia, which are known collectively as the Council's Constituent Bodies. The Law Council's Constituent Bodies are:

- Australian Capital Territory Bar Association
- Australian Capital Territory Law Society
- Bar Association of Queensland Inc
- Law Institute of Victoria
- Law Society of New South Wales
- Law Society of South Australia
- Law Society of Tasmania
- Law Society Northern Territory
- Law Society of Western Australia
- New South Wales Bar Association
- Northern Territory Bar Association
- Queensland Law Society
- South Australian Bar Association
- Tasmanian Bar
- Law Firms Australia
- The Victorian Bar Inc
- Western Australian Bar Association

Through this representation, the Law Council effectively acts on behalf of more than 60,000 lawyers across Australia.

The Law Council is governed by a board of 23 Directors – one from each of the constituent bodies and six elected Executive members. The Directors meet quarterly to set objectives, policy and priorities for the Law Council. Between the meetings of Directors, policies and governance responsibility for the Law Council is exercised by the elected Executive members, led by the President who normally serves a 12 month term. The Council's six Executive members are nominated and elected by the board of Directors.

Members of the 2018 Executive as at 1 January 2018 are:

- Mr Morry Bailes, President
- Mr Arthur Moses SC, President-Elect
- Mr Konrad de Kerloy, Treasurer
- Mr Tass Liveris, Executive Member
- Ms Pauline Wright, Executive Member
- Mr Geoff Bowyer, Executive Member

The Secretariat serves the Law Council nationally and is based in Canberra.

About the Section

The Legal Practice Section of the Law Council of Australia was established in March 1980, initially as the 'Legal Practice Management Section', with a focus principally on legal practice management issues. In September 1986 the Section's name was changed to the 'General Practice Section', and its focus broadened to include areas of specialist practices including Superannuation, Property Law, and Consumer Law.

On 7 December 2002 the Section's name was again changed, to 'Legal Practice Section', to reflect the Section's focus on a broad range of areas of specialist legal practices, as well as practice management.

The Section's objectives are to:

- Contribute to the development of the legal profession;
- Maintain high standards in the legal profession;
- Offer assistance in the development of legal and management expertise in its members through training, conferences, publications, meetings, and other activities.
- Provide policy advice to the Law Council, and prepare submissions on behalf of the Law Council, in the areas relating to its specialist committees.

Members of the Section Executive are:

- Mr Philip Jackson SC, Chair
- Ms Maureen Peatman, Deputy Chair
- Mr Michael James, Treasurer
- Ms Tanya Berlis
- Mr Dennis Bluth
- Mr Mark Cerche
- Dr Leonie Kelleher OAM
- Mr Geoff Provis

Acknowledgement

This submission has been prepared by the Law Council of Australia's Consumer Law Committee (**the Committee**), which is a committee of the Legal Practice Section of the Law Council of Australia.

Introduction

1. This submission has been prepared by the Law Council of Australia's Consumer Law Committee (**the Committee**), which is a committee of the Legal Practice Section of the Law Council of Australia.
2. The Committee is grateful for the opportunity to provide this submission to the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry (**the Commission**) regarding the document 'Policy Questions arising from Module 6'. The Committee has responded to a number of the Policy Questions raised.

Product Design

Policy Question 2

Are there particular products – like accidental death and accidental injury products – which should not be sold?

3. Yes, products which provide little to no benefit to consumers.
4. In the Committee's view, the current proposed Product Intervention Powers are not broad enough to ensure that the sale of entire categories or classes of products will be prohibited. The proposed version in Australia is a 'watered-down' version requiring the Australian Securities and Investment Commission (**ASIC**) to undertake extensive consultation without any power to make permanent rules. The proposal is, in a sense, 'the worst of both worlds'.
5. The regulator should be able to intervene and prohibit the sale of classes of products on all financial products as defined under the *Australian Securities and Investments Commission Act 2001*(Cth) (**ASIC Act**), where there is consultation and clear evidence of poor, ongoing consumer outcomes. Low claims ratios could be used as the basis for triggering intervention.

Disclosure (and Insurance in Superannuation)

Policy Questions 5, 6, 23 & 24

6. The Standard Cover regime in Division 1 of Part V of the *Insurance Contracts Act 1984* (Cth) (**ICA**) should be extended to cover life insurance contracts. In the Committee's view, should life insurance contracts become 'prescribed contracts' within the meaning of the ICA, there would be greater protection to consumers from harsh or unfairly restrictive definitions, and greater obligations placed on insurers to ensure that consumers are clearly informed of any deviation from the Standard Cover definition.
7. Group life insurance through superannuation is provided as a default product under the MySuper regime. Over recent years there has been significant changes to group life insurance policies across the superannuation industry. Those changes are invariably to make the definitions more onerous or harsh for a consumer. For example, Australian Super, one of Australia's largest superannuation funds, changed their definition of 'total and permanent disablement' (**TPD**) such that it now requires a member to prove that they are:

incapable of ever working in any job that ... [they are] reasonably suited to based on ... previous education, training or experience, or any job that [they] may reasonably

*become suited to with further education, training or experience within a reasonable period.*¹

8. Another example is the current insurance policy offered by MTAA Superannuation which defines regular and ongoing care as when the person:

(a) is under the regular and ongoing care of a medical practitioner who has given a clear prognosis that the Injury or Illness will continue throughout the life of the Covered Person (including after the expiry of the cover and the commencement of retirement) without any prospect of an improvement which would lead to a return to work (whether or not for reward) in any capacity; and

(b) is complying with reasonable medical advice and treatment; and

*(c) has, in our opinion reached the maximum level of medical improvement possible for that Covered Person based on their Injury or Illness.*²

9. In particular, clause a. above is a significant departure from the requirements under regulation 1.03C of the *Superannuation Industry (Supervision) Regulations 1994* (Cth) (**SIS Regulations**) and would mean that a member of that fund will be at a significant disadvantage to members of other superannuation funds which retain a definition consistent with the SIS Regulations.

10. It is submitted that significant benefit to consumers and industry would arise from having standard definitions in respect of, for example, TPD. Those benefits include:

(a) an existing body of jurisprudence in respect of the meaning of permanent incapacity/TPD, as defined in regulation 1.03C SIS Regulations;

(b) equity for all members of MySuper products who would have comparable quality of insurance cover;

(c) the ability to create industry wide standard claim forms, making the claims process more efficient; and

(d) greater efficiency in training of claims assessors who would only have to deal with a single definition across the industry.

11. Importantly, if the Standard Cover regime were extended to include life insurance there would be a need to amend section 37 of the ICA. It is well recognised and accepted that approximately 70 per cent of life insurance sold in Australia is sold through superannuation. Section 37 of the ICA obligates an Insurer to notify an 'Insured' in respect of any 'Unusual Terms'. However, where insurance is sold through a superannuation fund, the insured is the trustee, and the life insured or beneficiary is the member of the fund. Accordingly, the Committee proposes that section 37 should be amended to obligate an insurer to notify the insured and life insured or beneficiary of any unusual terms.

12. Currently, section 68AA of the *Superannuation Industry (Supervision) Act 1993* (Cth) (**SIS Act**) requires the trustee of a MySuper product to provide its members with an insured permanent incapacity benefit. For the purposes of section 68AA, 'permanent incapacity benefit' is defined as a benefit provided to a member of a fund 'if, *and only*

¹ Australian Super, *Insurance in your super: Money when it matters most* (27 October 2018) 24 <<https://www.australiansuper.com/campaigns/insurance-guide>>.

² MTAA Super, *Insurance Guide* (9 August 2018) 22 <<https://mtaasuper.com.au/-/media/consumer/files/disclosure/mtaa-super-guide-insurance-20180809.ashx?la=en>>.

if, the member is suffering permanent incapacity' (emphasis added). Permanent incapacity is defined under regulation 1.03C to mean:

if a trustee of the fund is reasonably satisfied that the member's ill-health (whether physical or mental) makes it unlikely that the member will engage in gainful employment for which the member is reasonably qualified by education, training or experience.

13. Accordingly, section 68AA operates such that it requires a trustee to provide a MySuper member with insurance cover which accords with the definition of permanent incapacity. However, as can be seen from the definitions referred to above, there is widespread derogation from the standard definition of permanent incapacity.
14. The Committee suggests that it would be in the interests of the industry and consumers to have standardised definitions for default insurance products, such as MySuper life and TPD insurance products. Importantly, insurers would be free to offer products with different insurance definitions subject to their obligation to clearly inform the insured of the unusual insurance terms. In addition, there is nothing that would prevent a consumer from seeking out an insurance policy with a different definition.

Sales

Policy Question 7

Should monetary and non-monetary benefits given in relation to general insurance products remain exempt from the ban on conflicted remuneration in Division 4 of Part 7.7A of the *Corporations Act 2001* (Cth)? If so, why?

15. No. The Committee's position is that these benefits should not be exempt as conflicted remuneration drives poor consumer outcomes and culture.

Policy Question 9

Is banning conflicted remuneration sufficient to ensure that sales representatives do not use inappropriate sales tactics when selling financial products? Are other changes, such as further restrictions on remuneration or incentive structures, necessary?

16. Banning conflicted remuneration is, however, not sufficient to ensure that sales representatives do not use inappropriate sales tactics when selling financial products.
17. The deferred sales mechanism for add-on sales is a particularly useful response to pressure selling where a consumer has not sought out an insurance product.
18. The Committee also submits that an outright prohibition on specific pressure sales tactics with appropriate monitoring enforcement and sanctions should be committed to under Codes of Practice applied to all distributors of insurance products.

Claims Handling – Life Insurance

Policy Question 19

19. The Committee supports the proposal to prevent a life insurer from denying a life insurance claim on the basis of a pre-existing condition in circumstances where the

claim is made in respect of a medical condition other than the pre-existing medical condition.

20. In the experience of the members of the Committee, there have been many examples where a life insurer has exercised a right to avoid a policy from inception on the basis of a pre-existing medical condition which is entirely unrelated to the medical condition on which the claim is based.
21. Section 29(3) of the ICA sets a low bar for the avoidance of a life insurance policy. That is so because the insurer need only show that they would not have entered into *the* life insurance contract (emphasis added). That is, if the insurer conducts a retrospective re-underwriting of the insurance policy and can show that it would have made any adjustment to the policy terms (i.e. a premium loading, an exclusion etc) then the insurer is entitled to avoid the policy. That is even so, where the medical condition which was not disclosed was entirely different to the condition being claimed for. That has a tendency to significantly advantage an insurer and disadvantage a consumer.
22. From a public policy perspective, it is, in the Committee's view, not equitable to have a situation in which an insurer enjoys the benefit of a premium, yet avoids any liability under the policy in circumstances where the insurer has suffered no detriment. That is, if the claimed condition is not in any way related to the alleged non-disclosure, then there doesn't appear to be any reason why the insurer should not provide the cover which the insured has paid for, often for many years.
23. A consumer receives some protection from the avoidance of a life insurance policy where the avoidance is harsh or unfair (section 31 of the ICA). However, the protections exist only where an insured is alleged to have fraudulently non-disclosed. That is, an insured who has innocently non-disclosed is not protected. In addition, the power conferred by the operation of section 31 is only conferred to a Court, and not to an External Disputes Resolution (**EDR**) Scheme, Tribunal or Ombudsman.

Insurance in Superannuation

Policy Question 28

Are the terms set out in the Insurance in Superannuation Voluntary Code of Practice sufficient to protect the interests of fund members? If not, what additional protections are necessary?

24. No. In the Committee's view the Insurance in Superannuation Voluntary Code of Practice (**the Code**) is not sufficient to protect the interests of fund members.
25. The Code is non-binding on members, unenforceable and has not been approved by ASIC to ensure that it meets the requirements as laid out in Regulatory Guide 183 (**RG 183**).
26. Other requirements, recommended by the Committee include:
 - strengthened commitments regarding cessation periods for all forms of default insurance within superannuation;
 - introduction of cessation periods for accounts with low contributions;
 - premium caps in line with the draft code released for public consultation in 2017, with a time-bound public commitment to review these caps to ensure they are set at appropriate levels for a basic default product;

- commitment to standardisation of insurance terms; and
- improved commitments with respect to claims handling and acting in the interests of the individual member.

Scope of the *Insurance Contracts Act 1984* (Cth)

Policy Question 29

Is there any reason why unfair contract terms protections should not be applied to insurance contracts in the manner proposed in “Extending Unfair Contract Terms Protections to Insurance Contracts”, published by the Australian Government in June 2018?

27. Unfair contract terms protections should be applied to insurance contracts regulated by the ICA.
28. The inclusion of unfair contract terms protections would complement the existing national framework for regulating unfair terms in consumer contracts. Central to that framework are the protections enshrined in:
- Part 2-3 of the *Australian Consumer Law (ACL)* regulating standard form consumer contracts; and
 - Subdivision BA of Division 2 of Part 2 of the ASIC Act which regulate most financial products and financial services.
29. The Committee regards the protections as a natural part of the evolution of the regulation of unfairness in contract terms in Australia. Those evolutionary steps have included:
- the historical recognition of various forms of unfairness by equity and the common law;
 - the enactment of legislation directed towards redressing unfairness in consumer transactions, including what was the *Trade Practices Act 1974* (Cth), and the state-based Fair Trading Acts;
 - the enactment of the *Contracts Review Act 1980* (NSW);
 - The introduction in 2003 of state-based unfair contract terms protections into the *Fair Trading Act 1999* (Vic);
 - The inclusion in the industry-based *Telecommunications Consumer Protections Code* (2007) of protections against the effects of unfair terms in consumer telecommunications contracts;
 - the enactment of Part 2-3 of the ACL which came into effect on 1 July 2010; and
 - the enactment of Subdivision BA of Division 2 of Part 2 of the ASIC Act which came into effect on 1 July 2010.
30. Unfair contract terms protections in insurance have recently been recommended by the Parliamentary Joint Committee on Corporations and Financial Services following its 2018 *Inquiry into the life insurance industry*,³ the Senate Economics References

³ Parliamentary Joint Committee on Corporations and Financial Services, Parliament of Australia, *Life Insurance Industry* (2018) recs 3.2, 8.6.

Committee following its 2017 inquiry into *Australia's general Insurance industry*,⁴ and the 2017 *Australian Consumer Law Review*.⁵

31. At present, section 13 of the ICA imposes a duty of utmost good faith. However, in practice the duty of utmost good faith does not protect a consumer from unconscionable, unfair or inequitable policy terms.
32. The Committee supports the proposal that the existing unfair contracts terms regime in the ASIC Act apply to insurance contracts regulated by the ICA, by the amendment of section 15 of that Act, as proposed in *Extending Unfair Contracts Terms Protections to Insurance Contracts: Proposals Paper* published by the Treasury in June 2018.⁶

Regulation

Policy Question 35

What is the purpose of infringement notices? Would that purpose be better achieved by increasing the applicable number of penalty units in section 12GXC of the *Australian Securities and Investments Commission Act 2001 (Cth)*? Should there be infringement notices of tiered severity?

33. Regulators should have sufficient tools available to them to efficiently penalise breaches of the law.
34. These penalties should not be capable of regulatory arbitrage or be seen as 'the cost of business' by financial firms. The regulator, in finding conduct that is a breach of the law, should have the capability to effectively penalise an entity. It may be appropriate to have tiers depending on the extent of the harm, the type of the business, the size of the business and the nature of the breach.

Compliance and Breach Reporting

Policy Question 39

Are there any recommendations in the "ASIC Enforcement Review Taskforce Report", published by the Australian Government in December 2017, that should be supplemented or modified?

35. Yes. The Committee generally supports:
 - (a) amending the misleading and deceptive conduct and unfair contract terms provisions to make them offence and civil penalty provisions;
 - (b) amending all ASIC-administered legislation to require the court when setting a penalty whether the penalty is sufficient to ensure deterrence and meet community expectations; and

⁴ Senate Economics References Committee, Parliament of Australia, *Australia's general insurance industry: sapping consumers of the will to compare* (2017) rec 11.

⁵ Consumer Affairs Australia and New Zealand, *Australian Consumer Law Review: Final Report* (2017) proposal 10.

⁶ The Treasury (Cth), *Extending Unfair Contracts Terms Protections to Insurance Contracts: Proposals Paper* (2018).

- (c) specifying that, in relation to a relinquishment order for breach of a civil penalty provision, a court can, in appropriate circumstances, order payment directly to the consumer.

36. Recommendation 18 of the ASIC Enforcement Review Taskforce (**Taskforce**) was that:

ASIC approval should be required for the content of and governance arrangements for relevant codes.

37. In the Committee's view, at a minimum ASIC must review and update RG 183 with mandatory requirements to capture the full spectrum of issues raised in the Royal Commission – particularly with respect to enforceability, sanctions powers, independent governance and its resourcing.

38. Consideration needs to be given to boosting enforceability and monitoring of these Codes beyond simple ASIC approval. Breaches of the Code need to include sanctions with 'bite' and should be a vital element of co-regulation to ensure that the commitments made by insurers in their Code are kept and that any breaches result in impactful consequences to motivate compliance.

39. Recommendation 20 states that

Approved codes should be binding on and enforceable against subscribers by contractual arrangements with a code monitoring body.

40. The Committee suggests that this needs to be enforceable as a term of the contract with consumers.

41. Recommendation 22 states that:

The code monitoring body, comprising a mix of industry, consumer and expert members, should be required to monitor the adequacy of the code and industry compliance with it over time, and periodically report to ASIC on these matters.

42. The Committee agrees with recommendation 22 and considers it important that a code monitoring body include consumer, industry, and expert views. Code monitoring bodies with diverse and inclusive representation are more likely to produce outcomes in which industry and consumers alike can have confidence.

43. Recommendation 36 states that:

Imprisonment should be removed as a possible sanction for strict and absolute liability offences.

44. The Committee disagrees with this recommendation and suggests that its implementation would send the wrong message. Section 190 of the *Corporations Act 2001* (Cth) (**Corporations Act**) currently bears imprisonment as a possible sanction for strict and absolute liability offences and even though the Attorney General's Department guide stipulates these offenses should not be punishable by imprisonment, removing this penalty altogether might undermine ASIC's prosecution of these offenses and signal the wrong culture.

45. Recommendation 45 states:

Infringement notices should be set at 12 penalty units for individuals and 60 penalty units for corporations for any new infringement notice provisions.

46. The Committee supports ASIC's proposal that all new infringement notice provisions in the Corporations Act should utilise the ration currently in use under the *National Consumer Credit Protection Act 2009* (Cth), being one-fortieth of the maximum penalty that a court could impose for civil penalty provisions.

Contact

47. The Committee would welcome the opportunity to discuss its submission further and to provide additional information in respect of the comments made above. In the first instance, please contact Mr Ben Slade, Chair, Australia Consumer Law Committee on (T) 02 8267 0914.