Chapter 6

Insurance consumers' interests

Introduction

6.1 The Committee understands that consumers of insurance products have fewer options in the current hard market because of reduced competition in the market place. This chapter discusses the relationship between the insurer and the consumer and considers whether measures to strengthen consumer protection are needed. Overall, the Committee in this chapter looks at:

- concerns about consumer interests and consumer protection; and
- the regulatory bodies that have responsibility for various aspects of the insurance industry including discussion of:
  - APRA's role,
  - the ACCC's role,
  - ASIC's role, and
  - the role of the insurers and the industry code of practice.

Assessment of premiums

6.2 One of the most persistent messages to emerge from this inquiry has been the confusion surrounding the assessment and pricing of premiums. Generally, witnesses were not only bewildered by the sudden and severe increase in premiums, despite relatively good claims history, but also by the growing use of clauses to exclude coverage of particular activities.

6.3 Dr Kenneth Baker, Chief Executive Officer, ACROD Ltd, told the Committee:

> There have been premium increases ranging from 30 per cent to, by today's evidence, 400 per cent. In some cases, organisations are having great difficulty getting any insurance cover at all. These refusals to insure and the great increases seem to be unrelated to the history of claims of the organisation. Organisations which may have been around for more than two or three decades and had no claims have nevertheless faced dramatic increases in premiums.[1]

6.4 The Royal Agricultural Society of Tasmania submitted that for the majority of Agricultural Societies in Tasmania there was no basis for premium increase which relates to the activities or heightened public risk in the conduct of their affairs. It

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1 *Committee Hansard*, 8 July 2002, p. 70.

maintained that in their case there had been no recent claims which could in any way have impacted on the increases quoted by the underwriters.[2] Similarly, the Australian Speleological Federation Inc. informed the Committee that in spite of a claimless record, its public liability insurance premium increased in 2002 from $4,500 to $18,000.[3]

6.5 The experience of the Australian Breastfeeding Association (ABA) highlights the experiences of many others. It stated:

> The threefold rise in our professional indemnity costs and doubling of public liability insurance premiums does not seem to reflect a realistic actuarial assessment of the actual risk associated with the ABA's activities. Rather, it seems that we are simply a low risk, small customer that does not contribute significantly to insurance company profitability.[4]

6.6 St John Ambulance Australia, the Australian Private Hospitals Association, Australian Nursing Federation, Outdoor Recreation Council of Australia Incorporated, Volunteering Australia, the Australian Rugby League, the Australian Cricket Board, the Australia Council, the Financial Planning Association of Australia and the Institute of Chartered Accountants are among the many witnesses who expressed concern that their risk assessment bore little relationship to the good rating in their claim records. They assert that insurers do not seem to take into account claims history in setting

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2 Submission 42, p. [3].

3 Submission 50, p. 1. See also submission 51, Illawarra Speleological Society, p. 1. The Australian Council of Professions Ltd cited a draft survey taken by the Australian Institute of Quantity Surveyors which indicated that quantity surveyors with no claims history have borne premium increases of between 50 and 200 per cent. It further shows that in five years only six insurance claims proceeded to court or arbitration and the total payout on claims was just $585,000 yet they were paying total premiums of $2 million a year.

4 Submission 64, p. 7. See also Mr Raymond Jones, President, Insurance Council of Australia Ltd, who acknowledged that 'There are a lot of very innocent victims out there who are being penalised for poor performance and poor risk management on behalf of similar organisations or similar companies across Australia. There are some very innocent adventure risk people who do manage their business very well. The insurance industry has never been able to go down to a one-on-one individual risk level.' *Committee Hansard*, 8 July 2002, p. 57.

premiums.[5] CPA Australia stated bluntly that underwriters 'are picking and choosing clients without regard for previous good risks.'[6]

6.7 The Financial Planning Association of Australia also noted that coverage is being increasingly restricted with respect to policy wordings and endorsements as well as the introduction of new exclusions.[7] The Institute of Chartered Accountants agreed with this view. It submitted:

> There is clear evidence that professional indemnity insurance is being offered on increasingly restrictive terms by insurers. In some cases, feedback from members has raised concern that up to 90% of a firm's activity could essentially be uninsured because it falls under one or another exclusion clause contained in the insurance contract.
>
> …
>
> Considerable uncertainty surrounds a number of new exclusions and as a consequence members do not know to what extent they are protected by their insurance policy.[8]

6.8 Moreover, the failure of the insurance companies to communicate effectively and openly with consumers about premiums has generated unnecessary disquiet at a time of difficulty in the industry.

6.9 Mr Gregory Nance from the Surf Life Saving Association stated simply 'I have never had adequately explained to me how insurers assess the amounts for premiums'.[9] Similarly, Mr Michael Potter from the Council of Small Business Organisations of Australia called for transparency in the process. He stated, 'Tell us, as the people who are basically going to be paying the premiums, how you came up with your actual premium content—where is the risk and where do you see the value of the claim?'[10]

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5 Submission 65, St John Ambulance Australia, p.[2]; submission 68, Australian Private Hospitals Association Limited, p. 3; submission 70, Australian Nursing Federation, p. [2]; submission 73, Outdoor Recreation Council of Australia Incorporated, p. [1]; submission 77, Volunteering Australia, p. 9; submission 82, Australian Rugby League Limited, p. 1; submission 94, Financial Planning Association of Australia Limited, p. 8, submission 95, Institute of Chartered Accountants, p. 8; submission 100, Australian Cricket Board, p. 2; submission 112, the Australia Council, executive summary. See also The South Australian Country Women's Association Incorporated, submission 17, p. 1; submission 129, Outdoors WA, p. [2]; submission 92, Logikal Health Products, p. 1; submission 96, Australian Council of Social Service, p. [2]; submission 97, Queensland Tourism Industry Council, p. 1. This list does not include all submissions that commented along similar lines.

6 Submission 125, CPA Australia, p. 3.

7 Submission 94, Financial Planning Association of Australia Limited, pp. 8–9.

8 Submission 95, Institute of Chartered Accountants, p. 7.

9 *Committee Hansard*, 8 July 2002, p. 3.

10 *Committee Hansard*, 9 July 2002, p. 93. See also Ms Sha Cordingley, Chief Executive Officer, Volunteering Australia, *Committee Hansard*, 10 July 2002, p. 176; Dr Rhonda Galbally, Chief

6.10 Some witnesses were asking that associations or other representative bodies have access to the claims history of their respective profession, trade or activity.[11] The Association of Independent Schools of South Australia submitted that the insurance industry should be required to be more transparent in explaining the increased cost of insurance premiums.[12]

6.11 A number of witnesses were not only troubled by the lack of explanation for higher premiums and the use of exclusion clauses but they also mentioned the lack of regard and fairness shown by insurers. Mr Paul Orton, General Manager Policy, Australian Business Ltd, told the Committee that a number of brokers in dealing with insurers had found a certain sense of indifference about 'the difficulty that the ultimate consumers of insurance products are facing'. He noted that that indifference is 'reflected in the lack of rationale for knockbacks for the retention of what had been long held cover with a particular firm'.[13]

6.12 Mr Stephen Ball, Director, National Insurance Brokers Association, pointed out the hard reality of the insurance business. He explained:

> In a market of abundant supply, insurers would say. 'I don't really want to do that but, to be able to secure the premium placement, I will give you cover for that risk.' In a market of contracted supply, they will say 'Sorry, I don't really want to provide that cover any more.'[14]

6.13 While most acknowledged that insurance companies operate in a commercial environment and are accountable to their shareholders, they found difficulty in accepting the high increases and the lack of consideration. A number harboured suspicions that the increases were not solely the result of rising claim costs but were

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Executive Officer, Our Community, *Committee Hansard*, 10 July 2002, pp. 183–4, 186; Ms Karen Curtis, Director, Industry Policy, Australian Chamber of Commerce and Industry, *Committee Hansard*, 10 July 2002, p. 237. Dr David Stephens, Policy Consultant, Australian Council of Professions Ltd, called for better information to be provided particularly the reasons for rises. He told the Committee, 'The discipline of requiring in some way—whether through self-regulation or some other way—an insurance company to specify what component of a rise was attributable to what cause we think would make a hell of a difference in this field.' *Committee Hansard*, 8 July 2002, p. 41. Australian Business Ltd endorsed the need for insurance companies to open their books on a confidential basis to assist in the identification of the causes of rising premiums. It also suggested that, 'At the very least insurers need to be encouraged to embark on a communication campaign which explains to their customers why individual risk circumstances may be irrelevant in assessing the level of premium for public liability and professional indemnity insurance. Australian Business Limited, submission 115, p. 4.

11 See for example, submission 102, Royal College of Nursing Australia, p. 4. See also submission 142, Australian Institute of Quantity Surveyors, p. [3].

12 Submission 85, p. 6.

13 *Committee Hansard*, 8 July 2002, p. 64. See also statements by Stephen Harrison, Institute of Chartered Accountants, *Committee Hansard*, 8 August 2002, p. 308.

14 *Committee Hansard*, 9 July 2002, pp. 103–4. See also Dr Paul O'Callaghan, President, Australian Horse Industry Council, *Committee Hansard*, 10 July 2002, p. 262.

related to attempts to recoup other business losses. A number of sporting and charitable organisations felt strongly that it was 'unjust and inappropriate to seek to recover losses from sporting, charities and not-for-profit sectors of the community'.[15]

6.14 The Australian Council of Professions asked whether professions with low numbers of claims were effectively cross-subsidising claims by professions and by other insurance clients in sectors where claims and litigation were more common. Similarly, Volunteering Australia believes that they may be bearing the costs of others' liabilities.

6.15 This suggestion of cross subsidy was made in numerous other submissions often accompanied by a request for an investigation into the pricing of premiums.

6.16 The Australian Council of Professions suggested that it would be an appropriate subject for APRA or other relevant bodies to investigate. It went on to state:

> To the extent that claims history *does* influence premium rises, APRA could also look into whether the 'targeting' of insurance claims, and thus their impact on premiums is being driven more by the capacity to pay rather than by responsibility for the damage or loss.[16]

6.17 As well as an independent investigation of the pricing process, witnesses also wanted the insurance industry to take steps to improve the way companies determine premiums. Some wanted changes and were asking for the levels of risk in the various workplaces or activities undertaken to be assessed and the premiums adjusted accordingly.

6.18 Sport Industry Australia suggested that the Government should 'require insurance companies to review the process by which they assess the true risk of individual organisations to ensure it is fair and equitable, and reflects the true risk of the sport'.[17] Likewise, the Institution of Engineers recommended that the insurance industry change the way its costs premiums. It stated that currently, costs are spread across the board for all types of insurance. It suggested that premiums be structured so that everybody pays different rates according to their risk profile and claims history. The Institution submitted that only through 'a consistent Australia-wide approach can an effective solution to the complex problem of liability be solved.'[18]

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15 See for example, submission 44, Sport Industry Australia, p. 3; submission 77, Volunteering Australia, p. 9; submission 71, Our Community, p. [2].

16 Submission 55, 12.

17 Submission 44, p. 3. See also, submission 90, Australian Chamber of Commerce and Industry, p. 6.

18 Submission 81, p. 3. Mr Neil Coulson, Chief Executive Officer, Victorian Employers Chamber of Commerce and Industry, suggested that the insurance industry become more innovative in its approach. *Committee Hansard*, 10 July 2002, p. 232.

6.19 The general thrust of the need for improvement in the insurance industry focused on the principles of transparency, fairness and equity. The Australian Institute of Quantity Surveyors suggested that governments consider legislating to prevent the unfair penalizing of low risk professions in relation to both professional indemnity and public liability insurance.[19]

6.20 The Real Estate Institute of Australia proposed that the 'Federal Government initiate consistent and meaningful measures to ensure that there is a proper balance in professional indemnity insurance between realistic premiums and small business confidence that they are satisfactorily covered under insurance'.[20]

Committee's view

6.21 The Committee believes that at the moment consumers, in many cases, are not receiving adequate explanation for the increase in premiums or the refusal by an insurer to cover particular services or activities. This has been acknowledged by some companies in the industry. The Committee believes that consumers deserve to be better informed about the reasons for the increase or for the withdrawal of coverage. It accepts the view that the insurance industry needs to improve the provision and clarity of information they provide to consumers, which would include offering clear explanations for increases, providing pricing trend data, improving query and complaint handling systems, and using Plain English and standard terms in policies.[21]

Unfair advantage

6.22 Criticism of the insurance industry, however, extended beyond the paucity of information regarding the pricing of premiums and the actual method of assessing premiums. The Committee also received reports of insurance companies using unfair tactics, such as unreasonable timeframes in which to accept increased policy quotes. Ms Monica Persson, Executive Manager, Audiological Society of Australia, told the Committee that their organisation had been deliberately hindered in their efforts to access alternative cover. She explained that their insurer had:

> …been tardy in providing documentation upon which another insurer can assess our potential risk. By delaying the provision of appropriate documentation, they have, in effect, deprived us of the opportunity to negotiate alternative insurance options for our members, leaving our members in a potentially precarious position as they try to find insurance cover in order to continue to practise.[22]

6.23 Members of the Australian College of Midwives Inc had similar experiences. Mrs Alana Street, Executive Officer, explained that they had had a successful

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19 Submission 142, Australian Institute of Quantity Surveyors, p. [3].

20 Submission 91, p. 4.

21 Submission 55, Australian Council of Professions, p. 17.

22 *Committee Hansard*, 8 July 2002, p. 34.

arrangement with their insurer for some years. Initially, little notice was given of the insurer's intention to withdraw from the market. Mrs Street explained that:

> We had to contact them directly to ask them to 'please explain'. It took them two weeks to contact us by letter, explaining that the reason for their decision was a commercial one. We asked for evidence to support their decision, and they chose not to provide any. We feel there is no evidence, financial or otherwise.[23]

6.24 Mr Stephen Harrison, Chief Executive Officer, Institute of Chartered Accountants in Australia, also commented on the inadequate notification given to renew their cover. He told the Committee that:

> Despite the advanced notice that they gave over the renewal process and starting that process with the brokers and, presumably, the brokers with the underwriters, advice about renewal terms was left until the last 24 or 48 hours, leaving some firms either the option of taking those terms without the ability to renegotiate with another company or risking going bare for a period.[24]

6.25 Mr Leonard Earl, Member, Public Indemnity Insurance Panel, Institute of Actuaries added that brokers generally have been concerned about the lateness with which underwriters have provided them with terms. He told the Committee that some people receive their renewal terms very late and with restrictions on the various forms of coverage. According to Mr Earl this situation has caused great angst and concern for many. In his words, 'Suddenly, they find themselves without coverage in certain areas of practice or with draconian terms'.[25]

6.26 In responding to a question about the problems facing some in renewing their insurance cover, Mr Raymond Jones, President, Insurance Council of Australia, told the Committee:

> Rationalisation in the insurance broking sector of our industry is also happening, and it is badly needed. A lot of the problems and publicity that has been given to risks that have been hard to place and have not been put away on time are because you have a lot of small suburban brokers out there who are really being challenged by a very difficult environment. The big professional brokers are very quick to get in touch with us and communicate on issues, and we work closely with them. But a lot of these small brokers are really having trouble.[26]

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23 *Committee Hansard*, 10 July 2002, pp. 256-7.

24 *Committee Hansard*, 8 August 2002, p. 307.

25 *Committee Hansard*, 8 August 2002, p. 308.

26 *Committee Hansard*, 8 July 2002, p. 59.

6.27 While agreeing that the insurance market was experiencing trouble in adjusting to the changed circumstances, Mr Earl placed a different slant on the reasons for poor service. He told the Committee:

> …many experienced people left the industry as a result of mergers and amalgamations over the last 10 years, so we have many people who have never really gone through a hard market such as we are seeing now, which is probably the most volatile that I have seen in 30-odd years in the business. They just do not know how to manage the market.[27]

Committee's view

6.28 The Committee accepts that the insurance industry is having difficulty adjusting to current conditions. However it is concerned at the many reports it has received of what seems to be inappropriate or exploitative conduct by insurers, particularly in relation to last minute offers of renewal on exorbitant terms. The Committee considers that at the least insurers should be obliged to give 14 days notice of proposed terms of renewal or proposed refusal to renew a policy.

6.29 Section 58 of the *Insurance Contracts Act 1984* goes part way towards this. An insurer must, at least 14 days before expiry, advise 'whether the insurer is prepared to negotiate to renew or extend the cover'. Unfortunately this does not require the insurer (if it is inclined to negotiate) to make a firm offer at the time of giving notice. It leaves the way open for bargaining to continue up to moment of expiry—a situation which, in current conditions, will naturally favour insurers. The Committee does not think this is adequate consumer protection. The Committee considers that the provision should be strengthened to require insurers to make a firm offer at the time of giving notice.

Recommendation 9

The Committee recommends that the Government propose an amendment to section 58 of the *Insurance Contracts Act 1984* to ensure that insurers must give at least 14 days notice of the proposed terms of a policy renewal or proposed refusal to renew a policy.

A captive market and consumer concerns

6.30 Ms Lynne Curran from Treasury pointed out that if the insured is 'dissatisfied with the service that it is getting from an insurance company, it can always go to another insurance company'.[28]

6.31 While agreeing in part with this view, Mr West from Royal and SunAlliance placed the problems facing consumers in the context of today's market. He stated:

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27 *Committee Hansard*, 8 August 2002, p. 308.

28 *Committee Hansard*, 8 August 2002, p. 341.

> …if people do not like the premium from one insurer, they have been able to just go to another insurer, get another premium and maybe find it lower. There has not been the need for that same rigour. Obviously, the liability issue has made that significantly more difficult for people. It is also more difficult as to how you regulate free enterprise in terms of how it prices individual risk.[29]

6.32 Clearly, in the current market, the option for dissatisfied customers to take their business elsewhere is limited. As mentioned earlier, for some it is a captive market and under such market conditions the need for consumer protection increases.[30]

Committee's view

6.33 The Committee accepts that at the moment consumers looking for liability coverage do not have the degree of choice they may have had a few years ago. Evidence presented to the Committee shows that the current situation has certainly brought to the fore the issue of consumer protection particularly in the area of setting premiums.

6.34 The following section of the chapter looks at consumer protection matters and the regulatory bodies relevant to the insurance industry.

Current reviews—the ACCC and the Productivity Commission

6.35 As mentioned in the report, a number of current reviews of various aspects of the insurance industry are underway. Two of particular relevance to consumer protection are: the one being undertaken by the ACCC and the other by the Productivity Commission.

6.36 On 30 May 2002, the Minister for Revenue and Assistant Treasurer, Senator Helen Coonan, announced that the ACCC would monitor 'market developments and premium prices and that the Commonwealth would review the ACCC's involvement if it becomes clear the cost savings being made are not being passed through to consumers'. She stated that the Commonwealth would provide ACCC with a standing brief to continue to update its report on a six monthly basis over the course of the next two years.

> This ongoing monitoring role will enable an assessment of whether the insurance industry is adjusting premiums to take account of cost savings, and provide the gauge for the effectiveness of measures taken on a national basis to stabilise and contain management costs as reflected in public liability premiums.[31]

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29 *Committee Hansard*, 9 August 2002, p. 354.

30 See paragraphs 1.49–51.

31 Senator the Hon Helen Coonan, Minister for Revenue and the Assistant Treasurer, Joint Communique, Ministerial Meeting on, Public Liability, Melbourne, 30 May 2002.

6.37 The updated report was expected to be completed by July 2002.

6.38 On 26 July 2002, the Parliamentary Secretary to the Treasurer, Senator Ian Campbell, asked the Productivity Commission to undertake a research study into Australian insurers' claims management practices in the public liability class of insurance and benchmark them against world's best practice. In undertaking the study, the Commission is to have regard to a number of aspects dealing mainly with claims costs such as the impact of litigation on claims costs, the proportion of claims settled out of court, and the time taken to finalise claims. It is also to have regard to any connection between claims management practices and the affordability, and the availability of public liability insurance.[32]

6.39 The Commission is to report by 31 December 2002.

Committee's view

6.40 The Committee welcomes both reviews and recommends that their findings be made available to the public.

Recommendation 10

Noting that the first update of the ACCC's insurance industry market pricing review was made public in September, the Committee recommends that all subsequent six monthly reports be made public pursuant to section 27B of the *Prices Surveillance Act 1983.*

6.41 Although the reviews will provide information and improve transparency in the industry, the Committee notes that their role is limited to review not enforcement. In particular, the Committee notes that the ACCC, at the moment, has no power to ensure that savings from reforms currently being implemented are passed on to consumers.

6.42 The ACCC, however, may intervene under the Trade Practices Act if anti-competitive conduct is thought to be involved. It cannot initiate action for the purpose of ensuring that cost savings being achieved through current reforms are being passed through to consumers. The Committee does note, however, that Senator Coonan in the Joint Communique stated that the Commonwealth will 'review the ACCC's involvement (including more formal processes) if it becomes clear that cost savings are being made but not passed through to customers'.[33]

6.43 An example of a measure that the Commonwealth could take, and for which there is a precedent with the introduction of the GST, is to introduce price exploitation legislation. Such a measure would build into the Trade Practices Act a requirement

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32 Productivity Commission, Public Liability Claims Management, Terms of reference, http://www.pc.gov.Australia/research/studies/insurance/tor.html (15 August 2002).

33 Senator the Hon Helen Coonan, Minister for Revenue and the Assistant Treasurer, Joint Communique, Ministerial Meeting on Public Liability, Melbourne, 30 May 2002.

that businesses do not engage in price exploitation as a result of the implementation of reforms designed to lower the cost of insurance premiums.[34] Penalties would apply for breaches of the legislation.

6.44 The ACCC would also have the responsibility to educate and inform business and consumers about their rights and obligations under the proposed price exploitation legislation. It could undertake activities, as it did with the GST, such as establish a price 'hotline', which would allow consumers to alert the ACCC to any unjustified price increase in insurance premiums, as well as develop an information network database of consumer, community and volunteer groups, businesses and organisations.[35]

6.45 The Committee believes that under such legislation, the ACCC would be an effective force in protecting consumers from exploitation by ensuring that insurers pass on the full benefits of any savings due to law reform designed to reduce the costs of claims.

Recommendation 11

The Committee recommends that the Trade Practices Act be amended to allow the ACCC to take enforcement action to ensure that any savings or benefits that accrue directly or indirectly from legislative reforms being implemented throughout Australia to minimise insurance premiums are passed on by the insurance companies to consumers.

6.46 While the Committee believes that the reviews are important, they do not address the problems raised by witnesses about the actual method of assessment of premiums and whether unfair cross-subsidisation is occurring. In other words, they do not deal directly with the lack of transparency, fairness and equity in the assessment of premiums. The studies also do not appear to take account of some of the consumer interest matters raised by witnesses such as the imposition of unrealistic deadlines to renew insurance coverage.

Market integrity, consumer protection and the regulators

6.47 At the moment there are three main regulatory bodies responsible for monitoring and regulating various aspects of the insurance industry in Australia—APRA, the ACCC and ASIC. A number of witnesses, however, spoke of the

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34 See Part VB—Price exploitation in relation to A New Tax System, *Trade Practices Act 1974*. The legislation confers on the ACCC a number of statutory responsibilities including—to formulate guidelines, to issue a Notice when it considers a business has contravened the prohibition on price exploitation, to take court enforcement action, to monitor prices and to report to the Minister. See also, the ACCC, *Price Exploitation and the New Tax System*, http://gst.accc.gov.au/publications/24mar_final.htm (25 August 2002).

35 For more information on the work of the ACCC under Section 75AZ of the *Trade Practices Act 1974,* see *Report to the Minister Under Section 75AZ of the Trade Practices Act 1974, 1 April to 30 June 2001, and 1 July to 30 September 2001.*

confusion that exists in ascertaining the particular area of responsibility covered by the respective bodies. In commenting on the monitoring and complaints process, Dr Rhonda Galbally, Chief Executive Officer, Our Community, told the Committee that their organisation was 'very unclear about where complaints should go and how they could be dealt with'.[36]

6.48 Dr David Stephens, Policy Consultant, Australian Council of Professions, also told the Committee that one of the difficulties they have is determining who is responsible for matters such as consumer protection.[37]

6.49 Ms Sue Weston, General Manager, Office of Small Business, Department of Industry, Tourism and Resources, acknowledged that one of the main areas of complaints raised by small business was the lack of timeliness in notifying a consumer that cover was not being renewed. She, however, was uncertain of where such a complaint could be taken. She told the Committee 'we need to have a look at the extent to which there is any mechanism they feel they can go to complain'.[38]

6.50 The Committee now looks at the role of the three regulatory bodies involved in the insurance industry with particular emphasis given to consumer protection issues.

APRA

6.51 Under legislation, APRA is established for the purpose of prudentially regulating bodies in the financial sector, which includes general insurance, and for developing the policy to be applied in performing that regulatory role. In providing regulation and developing policy, APRA is to balance the objectives of financial safety and efficiency, competition, contestability and competitive neutrality.

6.52 As mentioned earlier, one of APRA's key responsibilities is to ensure the financial viability of insurance companies. It told the Committee:

> APRA is *inter alia* responsible for general insurance safety and soundness in the interests of policyholders, which is essentially a matter of helping keep insurance companies solvent and liquid, and thus able to pay claims as they become due. APRA does not regulate insurance prices (premium levels), as this would be inconsistent with the Australian tradition of financial deregulation over the past 20 years. Nor is APRA responsible for consumer protection matters more generally, these are the province of the Australian Securities & Investments Commission.[39]

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36 *Committee Hansard*, 10 July 2002, p. 186.

37 *Committee Hansard*, 8 July 2002, p. 42: 'I think we said that APRA, again, should investigate whether professionals with low numbers of claims are cross-subsidising claims by others'.

38 *Committee Hansard*, 8 August 2002, p. 314.

39 Submission 127, p. 1.

6.53 The Committee accepts that APRA does not have a consumer protection role apart from ensuring that insurance companies are able to meet claims. As discussed in the previous chapter, as part of its responsibility as a regulator, APRA collects and analyses data on the insurance industry. The Committee has already made recommendations in this area.

6.54 In regard to APRA's role as a prudential regulator, the Committee refers to APRA's recent performance which has drawn strong criticism. Media reports suggest that public confidence in APRA has suffered and that the failure of HIH further eroded APRA's credibility as a strong and active regulator.[40]

6.55 In August 2001, the then Minister for Financial Services and Regulation, Mr Joe Hockey, acknowledged that the management and regulation of general insurance had been subject to intense scrutiny from the media, State and Federal politicians and the community. During a keynote address, he told the audience that:

> The failure of HIH is clear evidence that our reforms to general insurance are absolutely necessary. It has also given us the opportunity to reflect on what additional improvements could be made.[41]

6.56 In turning to government reforms intended to improve and strengthen the insurance industry, Mr Hockey mentioned the introduction of the General Insurance Reform Bill 2001. He noted that the Government had decided to amend the Bill with a view to 'harmonise and improve enforcement capabilities across all APRA-regulated institutions'. He stated:

> It was decided to bring forward these particular amendments in response to APRA's dealing with HIH. The Act's current enforcement provisions lack flexibility and require the establishment of a high level of certainty by APRA before it can take appropriate action.[42]

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40 See for example: the *Age*, 'APRA hits back at critics over HIH' 26 June 2001; the *Age,* 'Ex-Treasury head takes aim at HIH', 10 August 2001; the *Advertiser,* "Financial authority 'too slow'"21 August 2001; the *Sydney Morning Herald,* 'Mystery why watchdog didn't bite', 1 September 2001; the *Western Australian,* 'Why weren't HIH bells loud, clear?', 1 September 2001; the *Sydney Morning Herald,* "HIH crash 'caught napping'", 4 December 2001; the *Australian Financial Review,* "HIH collapse signs 'relatively clear'", 4 December 2001.

41 Speech by the Hon Joe Hockey, Minister for Financial Services & Regulation, Keynote address for the ICA Canberra Conference, 9 August 2001.

42 Speech by the Hon Joe Hockey, Minister for Financial Services & Regulation, Keynote address for the ICA Canberra Conference, 9 August 2001. The Supplementary Explanatory Memorandum to the General Insurance Reform Bill 2001 stated that amendments to the enforcement provisions of the Insurance Act 'were not initially included in the Bill as they were to be considered in a separate process to update and harmonise enforcement and resolution of failure provisions across all Australian Prudential Regulation Authority regulated institutions'. It noted further 'following the failure of the HIH Insurance Group (HIH) it is proposed that some enforcement provisions that relate specifically to general insurance be brought forward for inclusion in the Bill'. The proposed amendments were 'to enhance APRA's investigative powers and its ability to gather information and issue directions to an entity'.

6.57 Also recognising the need to improve the regulatory regime under APRA, Mr Graeme Thompson, CEO of APRA, conceded in August 2001 that 'the few months since the HIH Insurance went into provisional liquidation have demonstrated sharply some of the perils of prudential regulation, as well as opening some opportunities for us'. He expected that the Royal Commission on HIH, would 'show that not only did APRA inherit a flawed regulatory system for general insurers, we inherited a deeply flawed company in HIH'.[43]

6.58 Concern about prudential regulation of the general insurance industry had been current for at least five years before then. Senator Conroy noted that 'In 1995, the ISC—the predecessor to APRA—first mooted changes to general insurance prudential standards….'

> So here is the key: in 1995, the ISC stopped talking about trying to lift the standard…After a lengthy period of consultation, APRA released a draft prudential standard on risk management for general insurers on 13 September 2000. It has taken five years for ISC and APRA just to get to the draft guideline.[44]

6.59 The Committee regrets that it took so long to establish a new prudential regulation regime. The General Insurance Reform Bill was passed on 29 August 2001 and received assent on 19 September 2001.

Committee's view

6.60 The Committee believes that in light of the recognised weaknesses in the regulatory system for the insurance industry, a close watch must be kept on the implementation of the legislative reforms recently introduced to the Insurance Act to ensure that they produce the intended benefits. The Committee also suggests that it is important for APRA to now prove itself as an effective and assiduous regulator in ensuring the prudential soundness of insurance companies. Its success in this area will help to better prepare those in the industry to adjust to changing market conditions and to prevent severe disruptions, such as the one Australia is currently experiencing. An efficient, strong and competent regulator will go some way to restore public confidence in the insurance industry.

Recommendation 12

The Committee recommends that the Government more actively monitor the activities of APRA and ensure that it has adequate powers and resources as well as a commitment to diligently supervise the industry.

6.61 The Committee also notes concerns that have been raised about organisations such as medical defence organisations that are outside APRA's purview.

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43 Graeme Thompson, 'APRA—3 years on', Speech, 9 August 2001.

44 Senator S. Conroy, *Senate Hansard*, 27 June 2001, p.25163.

Medical defence organisations (MDOs)

6.62 The National Farmers' Federation maintained that either medical defence funds are insurers or not. It stated:

> If they are insurers, they should be subject to the same requirements as other insurers, particularly prudential and reporting requirements. This could have prevented the collapse of UMP. On the other hand, if the defence funds are not insurers, it is not clear why doctors are allowed to practice without insurance.[45]

6.63 Mr Nigel Ray from Treasury explained to the Committee that medical indemnity is, indeed, different from other types of insurance. Their operations are formally conducted on a discretionary basis and so fall outside the APRA regulatory regime. He stated:

> As it is currently structured it is not technically insurance and it is not provided by insurance companies but, rather, by mutual structures—which…are called medical defence organisations. Unlike insurance products, which impose a contractual obligation upon insurance companies to honour a policy when an insured event takes place, doctors are covered by discretionary indemnity—that is, MDOs have an absolute discretion to deny cover in any circumstance.[46]

6.64 MDOs, at the moment, are not covered by the *Insurance Act 1973,* which has enabled them to do a range of things while not having to hold the sorts of reserves that the insurance companies are obliged to hold. Dr Robert Bain, Secretary General, Australian Medical Association, stated that the Association would like to see some:

> APRA requirements on the MDOs so that all of them have to meet minimum capital. There is also the question of common accounting standards. They have all adopted slightly different accounting conventions, with the most starkly different being at UMP, which had not brought the tail of what are called IBNR—incurred but not reported—incidents onto their balance sheet.[47]

6.65 The Insurance Australia Group agreed with the view of bringing medical defence organisations under the General Insurance Act. It stated:

> The same prudential and reporting standards should apply to all providers of general insurance, regardless of ownership structure, to ensure consistency

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45 Submission 123, p. 11.

46 *Committee Hansard*, 8 August 2002, pp. 321-2, 343.

47 *Committee Hansard*, 8 July 2002, p. 29. See also Dr Michael Sedgley, Chairman of Council, Australian Medical Association, who agreed that medical defence organisations should be more accountable to their members. *Committee Hansard*, 8 July 2002, p. 23.

> in the management of long tail classes and full funding of all premium pools.[48]

6.66 As part of the Government's longer term strategy to deal with the difficulties in the medical indemnity market, the Prime Minister, Mr John Howard, proposed on 31 May 2002 to improve transparency in the financial reporting of MDOs and to bring all of their insurance business into the prudential framework for general insurers.[49] This measure was only one key element in a number of proposals. He announced that it was the Government's intention that 'a new comprehensive framework of measures' would be in place before 31 December.

6.67 According to Mr Ray, the Department of the Treasury is currently consulting on the possible measures to bring MDOs into the APRA framework. As an example, Treasury is considering 'requiring their services, or at least their insurance-like services, to be offered via a contract of insurance'.[50]

Committee's view

6.68 The Committee supports the consultative process that is taking place and hopes that it will lead to better regulation of MDOs. The Committee, however, suggests that the current consultations take a broader view of insurance providers and, with a view to assessing the level of protection that they offer to Australian consumers, give consideration to unregulated state insurers, all mutual insurers and overseas insurers providing cover in Australia. By bringing all unauthorised and insurance-like providers under the purview of APRA, the regulator is better able to appreciate how the industry works as a whole including consumer protection matters.

ACCC

6.69 The ACCC is an independent statutory authority with responsibility for administering the *Trade Practices Act 1974* and the *Prices Surveillance Act 1983*. The Trade Practices Act covers matters such as anti-competitive practices, unconscionable conduct, industry codes, unfair practices, product safety and information and product liability. The Prices Surveillance Act has three main functions which in broad terms allow the ACCC, under certain circumstances, to vet proposed price rises, to hold inquiries into pricing practices and to monitor prices, costs and profits of an industry or business. [51]

6.70 The ACCC told the Committee that it has a 'fairly limited role in relation to insurance'. It noted that it has a reporting role which started in June 2001 when it was asked by the then Minister for Financial Services and Regulation, Mr Joe Hockey, to report on the general insurance industry and premium increases following the collapse

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48 Submission 143, p. 3.

49 Press Release, Prime Minister, *Medical Indemnity Insurance,* 31 May 2002.

50 *Committee Hansard*, 8 August 2002, p. 343.

51 For more detail see http://www.accc.gov.au/about/about.htm (25 August 2002).

of the HIH group of insurance companies. The ACCC reported in March 2002 and, as noted earlier, has been asked to update the report which it anticipated would be finalised by the end of July 2002. It is now available.[52] As already discussed, the ACCC has also been asked to monitor insurance premiums over a two year period and to report on whether they reflect the legislative changes that are currently being made or proposed by Commonwealth and state governments.[53]

6.71 The Committee, however, believes that more is required than simply monitoring and recommended earlier that the ACCC be given the authority to ensure that savings from reforms are passed on.

6.72 The evidence before this Committee clearly demonstrates that there is wide support for the work of the ACCC in monitoring insurance pricing.[54] ACROD submitted:

> The dramatic rise in premiums, the widespread refusal to renew or offer new public liability cover, the contradictory signals over profitability, the failure and collapse of several companies (apart from HIH), the uncertain consequences of current rationalisations and the industry's reluctance to disclose appropriate data—among many other things—all point to an industry in denial. Traditionally cloistered, the private insurance sector has unwittingly been subjected to critical public scrutiny. If only for the industry's own sake, a formal investigation of the more damaging aspects of recent developments should be undertaken. From the viewpoint of disability services, the most appropriate subject and mechanism would be an investigation by the ACCC into premium rises of above 25% in the non-profit sector. The purpose would be not so much to detect collusion as to explicate pricing policy.[55]

6.73 Mr Paul Orton, General Manager Policy, Australian Business Ltd, wanted the ACCC's role to be maintained so that they could be confident that 'we have a competitive public liability insurance market and that we see evidence of the state of competition through increased capacity coming into the industry and new products that better deal with particular sectoral insurance needs'.[56]

6.74 The ACCC informed the Committee that it has a role in relation to consumer protection provisions in the Trade Practices Act, notably, the warranty and liability provisions and the provisions relating to misleading or deceptive conduct.

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52 Australian Competition and Consumer Commission, *Second Insurance Industry Market Pricing Review,* September 2002.

53 Mr Brian Cassidy, Chief Executive Officer, ACCC, *Committee Hansard*, 9 July 2002, p. 111.

54 See for example, submission 55, Australian Council of Professionals Ltd, p. 17.

55 Submission 59, p. 11.

56 *Committee Hansard*, 8 July 2002, p. 69.

6.75 It is in this area of consumer protection that confusion exists about the precise responsibility of the ACCC. The ACCC, under the Trade Practices Act, is responsible for consumer protection generally, but excluding financial services. ASIC, under the ASIC Act, is responsible for consumer protection in relation to financial services—which includes insurance. In these Acts 'consumer protection' refers to controlling a variety of objectionable behaviours, of which the most important is 'misleading or deceptive conduct.' However, separate provisions apply to 'unconscionable conduct'. Both authorities have continuing responsibilities in relation to unconscionable conduct in the supply of financial services.[57]

6.76 This framework does not make it clear to whom consumers should complain when they feel that pricing for public liability and professional indemnity services is too high or inconsistent with previous prices or policy coverage. Given that the ACCC is already monitoring pricing within the public liability and professional indemnity insurance market to ensure market competitiveness, and the Committee has recommended the provision of enhanced enforcement powers (see paragraphs 6.43–45), it would be prudent for the ACCC to handle complaints alleging price exploitation. The additional information flow would provide a deeper understanding of the market and lead to greater competition.

6.77 In turning to the more general aspects of consumer protection, Mr Robert Antich from the ACCC explained that:

> Insurance is a part of the financial services role that ASIC now has after 11 March this year as part of the Financial Services Reform Act. In terms of insurance itself…we do not have a role in relation to consumer protection.
>
> …our understanding is that ASIC would have that primary responsibility in relation to consumer protection relating to insurance services.[58]

6.78 Mr Brian Cassidy, Chief Executive Officer, the ACCC, explained further that up till March, the ACCC would have potentially been able to take action in relation to conduct that was thought to be misleading or deceptive but that ASIC now had that role.[59] He also noted that the ACCC has joint responsibility with ASIC for the 'unconscionable conduct in business transactions provisions insofar as they relate to the provision of financial services'.[60]

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57 *Australian Securities and Investments Commission Act 2001*, Part 2, Division 2. *Trade Practices Act 1974*, Part IVA. In the Trade Practices Act one unconscionable conduct provision - s51AB - does not apply to financial services (it is replicated in s12CB the ASIC Act). Another unconscionable conduct provision - s51AC - is replicated in s12CC of the ASIC Act but also continues to apply in the Trade Practices Act.

58 *Committee Hansard*, 9 August 2002, p. 113.

59 *Committee Hansard*, 9 July 2002, p. 114.

60 *Committee Hansard*, 9 July 2002, p. 123.

6.79 Obtaining a clear understanding of who has responsibility for consumer protection in regard to insurance matters is complicated by the recent transfer of power to ASIC. Mr Antich explained:

> That has been a source of discussion between us and ASIC in relation to how this is handled. Obviously you will have investigations that will straddle that date; you will have conduct that will happen before and after that date [11 March 2002]. It is a very live issue and it is one we are well aware of. There is a process in place and dialogue with ASIC so we can have an orderly handover of those sorts of issues.[61]

6.80 Mr Sean Hughes from ASIC told the Committee that they are aware of a number of consumer concerns in relation to accessing cover and the terms in which the cover is offered. He told the Committee that they refer those consumers and those inquiries elsewhere—to the ACCC—because it is not within ASIC's bailiwick. Mr Peter Kell stated:

> It is the ACCC's jurisdiction to cover the general price issues, as long as the price is clearly and accurately disclosed and there is no misleading information given about it; those are the issues that we are concerned with.[62]

6.81 The confusion may in part stem from the statements concerned about consumer interests and protection made by the ACCC. For example in March 2002, the Chair of the ACCC, Professor Fels, suggested that consumers needed clear information about the increased charges for their individual insurance policies and that insurance companies should review and improve their inquiry and complaints handling systems to help consumers who want to query increases.[63]

6.82 The Committee endorses the views of Professor Fels. However, it is also evident that members of the public are not generally aware of the roles of the regulators in the general insurance market.

Committee's view

6.83 The Committee understands that the transfer of consumer protection responsibility in relation to financial services to ASIC was to ensure that ASIC would be concerned with all aspects of financial products. Thus, consumers would know that they could approach ASIC on any matter related to financial products. Despite this transfer of power from the ACCC to ASIC, the line separating them in their respective roles in consumer protection is not widely understood.

6.84 The Committee believes strongly that the roles of the ACCC and ASIC in relation to these matters must be placed beyond doubt.

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61 *Committee Hansard*, 9 July 2002, p. 123.

62 *Committee Hansard*, 9 August 2002, p. 384.

63 ACCC, Media Release, *Consumers Need Clear Insurance Information*, 26 March 2002.

Recommendation 13

The Committee recommends that, in close consultation, the ACCC and ASIC review and report publicly on their respective statutory obligations in regard to consumer protection and market integrity in the insurance industry with a view to:

- **clarifying their respective responsibilities, giving particular attention to whether there is any unnecessary overlap; and**
- **establishing whether, in their opinion, the legislation provides adequate and appropriate consumer protection in the insurance industry and, if not, identifying the gaps or weaknesses in consumer protection, including the prices and insurance coverage that are being offered to consumers.**

The Committee further recommends that the ACCC and ASIC actively promote their roles in consumer protection for all financial products, including general insurance.

ASIC

6.85 ASIC is an independent statutory body with the responsibility to enforce company and financial services laws to protect consumers, investors and creditors.[64]

6.86 The *Australian Securities and Investments Commission Act 2001* states clearly that ASIC has the function of monitoring and promoting market integrity and consumer protection in relation to the Australian financial system.[65] ASIC also has powers conferred on it by a number of other acts including the *Insurance Contracts Act 1984*.[66]

6.87 Under this Act, ASIC has the power to do all things that are necessary or convenient to be done in connection with the administration of the legislation. The Act is intended to ensure that 'a fair balance is struck between the interests of insurers, insureds and other members of the public and so that the provisions included in such contracts, and the practices of insurers in relation to such contracts, operate fairly, and for related purposes'.

6.88 Without limiting the generality of that power, ASIC has power *inter alia*:

- to promote the development of facilities for handling inquiries in relation to insurance matters;
- to monitor complaints in relation to insurance matters;

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64 For more details see: http://www.asic.gov.au/asic.nsf/byheadline/ASIC+at+a+glance?open document (25 August 2002).

65 Section 12A(3), *Australian Securities and Investment Commission Act 2001.*

66 Section 12A(1), *Australian Securities and Investments Commission Act 2001.*

- to monitor legal judgments, industry trends and the development of community expectations that are, or are likely to be, of relevance to the efficient operation of the Act; and
- to promote the education of the insurance industry, the legal profession and consumers as to the objectives and requirements of the Act.[67]

6.89 The Act clearly states that 'a contract of liability insurance is a contract of general insurance that provides insurance cover in respect of the insured's liability for loss or damage caused to a person who is not the insured'.[68] These responsibilities are consistent with ASIC's powers as defined in the *Financial Services Reform Act 2001* (FSR Act).

6.90 The new licensing and product disclosure regimes introduced under the FSR Act apply to insurance companies and insurance agents and brokers. ASIC informed the Committee that under the new legislation, an insurance company will need to hold an Australian financial services licence if it carries on a financial services business otherwise than as a representative of a licensee.[69] By the end of the two-year transition period, agents and brokers will need to be appropriately authorised as representatives of an Australian financial services licensee or need to hold an Australian financial services licence.

6.91 General insurance policies are deemed to be 'financial products'. Part 7.9 of the Corporations Act contains a number of requirements relating to financial product disclosure and the issue and sale of financial products. Most important is that 'regulated persons' are required to give a Product Disclosure Statement (PDS) to retail clients in certain situations, including where personal advice recommending the acquisition of a particular product is given, or where a person offers to issue or arrange for the issue of a financial product.

6.92 The PDS must contain sufficient information so that a retail client may make an informed decision about whether to purchase a financial product. The statement is to include information about fees payable in respect of a financial product, the risks and benefits of a financial product, and significant characteristics of a financial product.[70]

6.93 It does not appear, however, that public liability and professional indemnity insurance is subject to the disclosure provisions.[71]

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67 Section 11B, the *Insurance Contracts Act 1984,* compiled 11 March 2002.

68 Section 11.

69 Exemptions do apply such as bodies regulated by APRA if the service is one in relation to which APRA has regulatory or supervisory responsibilities and the service is provided only to wholesale clients.

70 Part 2, subdivision 2 C and D, *Australian Securities and Investments Commission Act 2001.*

71 See Appendix 7, additional information from ASIC, 2 October 2002.

Statutory dispute resolution procedures

6.94 Under the *Financial Services Reform Act 2001* (FSR Act) a licensee has certain obligations. Section 912A directs a licensee, if those financial services are provided to persons as retail clients, to have a dispute resolution system that complies with specified conditions set down in the legislation.[72] A dispute resolution system must consist of

a) an internal dispute resolution procedure that

i) complies with standards, and requirements, made or approved by ASIC; and

ii) covers complaints against the licensee made by retail clients in connection with the provision of all financial services covered by the licence; and

b) membership of one or more external dispute resolution schemes that:

i) is, or are, approved by ASIC.

6.95 Under section 915, ASIC may suspend or cancel the licence if the licensee has not complied with, or ASIC has reason to believe it will not comply with, its obligations which, as noted above, includes having a dispute resolution system.

6.96 Policy Statement 139, issued by ASIC, provides advice on how it approves external complaints resolution schemes operating in the financial system. It contains 'a common set of guidelines developed for broad application'. In accordance with this statement, ASIC approved a scheme in August 2000, known as the General Insurance Enquiries and Complaints Scheme, operated by Insurance Enquiries and Complaints Ltd (IEC), as an approved dispute resolution scheme.[73] IEC is an independent company funded by participating insurers. It receives about 90,000 to 100,000 inquiries per year.[74]

6.97 The Committee is concerned that both the disclosure requirements and dispute resolution provisions of the FSR Act do not effectively address the insurance problems revealed in the inquiry. Firstly, a dispute resolution scheme applies only to 'retail clients' as defined in the FSR Act. The definition is limited to individuals and small businesses, and is limited to their dealings in respect of certain listed classes of

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72 *Financial Services Reform Act 2001*, schedule 1 inserting s912A in the *Corporations Act 2001.*

73 PS 139.13, ASIC, Policy Statement139, Approval of external complaints resolution schemes, issued 8/7/1999, obtained from ASIC's website, 23 September 2002. See also ASIC http://www.asic.gov.Australia/fido/fido.nsf/byheadline/General=Insurance+Code+of+Practice (22 September 2002). See also Mr Peter Kell, ASIC, *Committee Hansard*, 9 August 2002, p. 379.

74 pers. comm. P. O'Connor, Public Affairs Manager, Insurance Enquiries and Complaints Ltd, September 2002.

insurance. The listed classes do not include public liability or professional indemnity insurance (though the list can be enlarged by regulation).[75] ASIC has advised the Committee that no regulations have been made under this section to include public liability and professional indemnity insurance.[76] Secondly, it is unclear whether a complaint about price exploitation in a proposed policy renewal is within scope; and if so, it is unclear whether IEC (which currently handles only disputes over claims) is equipped to deal with it.

6.98 The concerns about the possible inadequacy of the legislation are reflected in the terms of reference of the General Insurance Enquiries and Complaints Scheme. The terms identify certain classes of insurance, which includes professional indemnity insurance, that are outside the terms of reference. The omission of public liability from the insurances covered by the terms of reference suggest that this class of insurance is also excluded from coverage. Not only are the classes of insurance limited but those actually entitled to refer a dispute to the Scheme are also confined to include natural persons and parties who conduct a small business. The definition of small business is narrower than that given in the ASIC Act.[77]

6.99 Mr Peter Kell, ASIC, told the Committee that under the FSR Act, ASIC had asked IEC to reconsider their coverage of that scheme to ensure that it is compliant with the new regime. In particular, according to Mr Kell, they will have to ensure that they can deal with complaints about arguments about disclosure of premiums or costs, or arguments about incorrect information recorded about details that lead to disputes down the track when claims arise.[78]

6.100 The Committee, however, would like to see the matter given urgent attention. It believes that the scheme, as it now stands and approved by ASIC, fails to offer adequate consumer protection to a range of insureds.

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75 *Financial Services Reform Act 2001*, schedule 1 inserting s761G in the *Corporations Act 2001*. Section 761G—Meaning of retail client and wholesale client—specifies the classes of general insurance covered under the term retail client. Although public liability and professional indemnity insurance is not listed, subsection (viii) provides for the inclusion of a kind of general insurance product prescribed by regulations made for the purposes of this subparagraph.

76 See answer to question 1, Appendix 7, additional information from ASIC, 2 October 2002.

77 Section 1.2, the General Insurance Enquiries and Complaints Scheme, Terms of Reference, 1 May 2002. Section 761G(12), *Financial Services Reform Act 2001*, defines small business as a business employing less than 100 people if the business is or includes manufacture of goods, otherwise 20 people. The General Insurance Enquiries and Complaints Scheme defines small business as an individual, a partnership of natural persons or a corporation whose shareholders are natural persons; and which has no more than 5 employees (including working proprietors) at any one time; and has an annual turnover not exceeding $400,000.

78 Mr P. Kell, *Committee Hansard*, 9 August 2002, p. 379.

Committee's view

6.101 The Committee regrets that the statutory complaint-handling procedures now in place do not meet the needs of the groups most affected by the insurance crisis, particularly not-for-profit organisations. The Committee acknowledges the policy intent of the FSR Act that the complaint-handling procedure should be an additional protection available to retail but not wholesale clients.[79] However it is regrettable that not-for-profit organisations have been excluded from the definition of 'retail clients'. Furthermore, the Committee sees no logic in limiting the classes of insurance to which disclosure provisions or complaint-handling procedures apply.

Recommendation 14

- **The Committee recommends that the Government amend the FSR Act to allow not-for-profit organisations to be included in the definition of 'retail clients'.**
- **The Committee recommends that the Government, by regulation, include public liability insurance and professional indemnity insurance in the classes of insurance covered by the dispute resolution provisions of the FSR Act.**
- **The Committee recommends that ASIC monitor the effectiveness of the dispute resolution provisions and report on this annually to the Parliament.**
- **The Committee recommends that ASIC review, as a matter of urgency, the General Insurance Enquiries and Complaints Scheme and in consultation with the Insurance Council of Australia ensure that it covers adequately public liability and professional indemnity insurance and not-for-profit organisations. Further that it re-examine definitions in the terms of reference, such as small business, to ensure that they are consistent with definitions in Commonwealth legislation.**

General Insurance Code of Practice

6.102 Before changes to the *Australian Securities and Investments Commission Act 1989,* under section 12FA ASIC had the function of promoting the adoption of, and approving and monitoring compliance with, industry standards and codes of practice (including standards and codes in relation to the resolution of disputes between the providers of financial services and consumers).[80]

79 Financial Services Reform Bill 2002, explanatory memorandum, par. 6.10.

80 Australian Securities and Investments Commission Act 1989, compiled 19 July 2001.

6.103 Section 113 of the *Insurance Act 1973* also provided for ASIC to approve a code of conduct.[81] This section was repealed by the *Financial Services Reform (Consequential Provisions) Act 2001*.

6.104 Provisions to allow ASIC to approve codes of conduct have now been included in the Financial Services Reform Act.[82]

6.105 The General Insurance Code of Practice appears to offer another avenue for improving consumer protection. IEC is responsible for the administration of the code, which was approved by ASIC in August 2000. It is a self-regulatory code of practice to promote good relations between insurers, agents and consumers and good insurance practice by describing standards of good practice and service. The code requires participating insurers to establish internal and external dispute handling procedures and insurers may be penalised if they fail to meet the code's requirements.[83]

6.106 The Committee notes the principles espoused in the code, which include having regard to the duty of utmost good faith and the need for effective competition and cost efficiency being promoted in the general insurance industry. As well, the code directs insurers prior to each renewal 'to provide to consumers information on any changes to the policy being renewed in plain language and in a format aimed to assist comprehension by consumers'. The code states further that:

> Where an insurer declines cover or refuses to renew a policy because of factors that do not relate to the assessment of the particular risk (For example, the insurer has ceased to offer the cover) then the insurer shall notify the consumer of that fact.[84]

6.107 The code, however, is narrow in focus and has the same shortcomings as the General Insurance Enquiries and Complaints Scheme. The present Code of Practice is expressed to apply only to individuals, and only relating to insurance for private or

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81 *Insurance Act 1973, compiled 15 July 2001,* section 113, Compliance with codes of insurance practice, read:

(1) If:

a) a code or codes of practice have been approved by ASIC in relation to the carrying on of a class of insurance business prescribed for the purposes of this section; and

b) a person carries on that class of insurance business on a day when the person is not a party to an agreement to comply with the code or one of the codes; the person is, in respect of that day, guilty of an offence punishable on conviction by a fine of not more than:

c) if the person is a body corporate—200 penalty units; or

d) if the person is a Lloyd's underwriter and is not a body corporate—20 penalty units.

82 Section 1101A, Approved codes of conduct*, Financial Services Reform Act 2001.*

83 General Insurance Code of Practice, http://www.ica.com.au/codepractice/introduction.asp (10 August 2002).

84 General Insurance Code of Practice, http://www.ica.com.au/codepractice/policy.asp (10 August 2002).

domestic use. This excludes not-for-profit-organisations and small businesses. The classes of insurance covered exclude public liability and professional indemnity.[85] There are no provisions for dealing with complaints about price exploitation in proposed policy renewals. Any one of these points would prevent the Code from being useful to the groups suffering most from the insurance crisis. The Committee sees no logical reason for these exclusions.

6.108 The code is subject to review every three years and a new exposure draft is expected to be released soon.[86] The Committee considers that the new code should address the above concerns. In particular, the Committee suggests that definitions in the code be expanded to ensure a more comprehensive coverage of insurance business. The definition of the business covered should be broadened to specifically include public liability and professional indemnity insurance.

6.109 The Law Council of Australia suggested that insurers ought to put into their voluntary code of practice some obligation to provide proper notification of substantial increases as well as a possible obligation not to increase premiums by more than a certain percentage unless there is a good underwriting reason.[87]

6.110 Actuarial advice provided by Cumpston Sarjeant Pty Ltd contained more specific suggestions. It recommended that the code include an objective that would 'require insurers to provide reasonable premium stability to existing clients, and to accept new clients at reasonable premiums'. It further suggested that a new section be inserted to the effect that:

> Insurers shall renew the insurance of an existing client, at a premium not more than 50% higher than the previous premium, unless there is evidence that the risks under the policy have materially changed, or there has been significant past misrepresentation.
>
> Insurers shall accept a new client, previously insured by another insurer, at a premium not more than 100% of the previous premium, unless there is evidence that the risks under the policy have materially changed, or there has been significant past misrepresentation.
>
> Insurers shall contribute underwriting and claims data to statistical schemes intended to provide reasonable claim cost estimates for different risks.[88]

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85 Other classes may be covered optionally by participating insurers (clause 2.1, definition of 'insurance business', item (c)). However the Committee understands that few if any participants take advantage of this clause, since most public liability or professional indemnity insurance buyers would in any case be excluded as not being individuals buying for domestic use.

86 Insurance Council of Australia, *Senator welcomes new code to improve insurance customer service*, media release 22 August 2002.

87 Mr Tony Abbott (Law Council of Australia), *Committee Hansard*, 8 August 2002, p. 269.

88 Submission 132, Law Council of Australia, attachment: Actuarial Advice by Cumpston Sarjeant Pty Ltd to Mr Tony Abbott, pp. 8–9.

Committee's view

6.111 The Committee does not adopt any particular detailed view on these points. It suggests, however, that the insurance industry and ASIC use such recommendations as a starting point to review the code.

Recommendation 15

- **The Committee recommends that the General Insurance Code of Practice be revised so that it provides remedies for community groups and small businesses that are affected by price exploitation in relation to public liability or professional indemnity policies.**
- **The Committee recommends that Insurance Enquiries and Complaints Ltd submit the revised code for ASIC's approval under the FSR Act.**

Insurance Ombudsman

6.112 Our Community recommended that 'serious consideration be given to the appointment of an Independent Insurance Industry Ombudsman with the power to investigate and decide on cases referred to it.' It suggested that such a measure would 'assist in ensuring that the introduction of tort reform by States leads to lower premiums.'[89]

Committee's view

6.113 The Committee believes that the establishment of an Insurance Ombudsman would add another level of bureaucracy to an already unclear situation. The Committee has already recommended that the ACCC should have increased powers to control price exploitation (see paragraph 6.45). This should include the collection of consumer complaints in regard to price and coverage. The Committee has also recommended the promotion of the respective roles of the ACCC and ASIC in the insurance market (see paragraph 6.84). These measures should significantly improve consumer protection and market integrity for all consumers.

SENATOR JACINTA COLLINS
Chair

89 Submission 71, pp. [4, 5].