Inquiry into Corporations Amendments Regulations Batches 6, 7 & 8

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Introduction and Summary

The Insurance Council of Australia (ICA) is the representative body of the general insurance industry in Australia. ICA members account for over 90 per cent of total premium income written by private sector general insurers.

ICA members, both insurance and reinsurance companies, are a significant part of the financial services system. Recently published statistics from the Australian Prudential Regulation Authority (APRA) show that the private sector insurance industry generates direct premium revenue of $19.8 billion per annum and has assets of $66.6 billion. The industry employs about 25,000 people.

ICA members issue some 37.8 million insurance policies annually and deal with 3.5 million claims each year.

ICA believes that the Corporations Amendments Regulations Batch 6, 7 and 8 should be reviewed as necessary and passed as soon as possible. This will give ICA members a degree of certainty that currently does not exist leading up to 11 March 2004.

There are two aspects on which ICA wishes to comment, one in Batch 6 related to radio advertising and one in Batch 8, the requirement to have ASIC determine if for a “compelling reason” disclosure may be made in other than dollar terms.

Corporations Amendments Regulations 2003 (Batch 6)

Section 1018A – Radio Advertising

Many ICA member companies advertise their financial products on radio, and are impacted by the provisions of Section 1018A of the Corporations Act, ("the Act"). ICA has been made aware of a number of possible unintended consequences arising out of or as a direct consequence of these particular product disclosure requirements.

Section 1018A of the Act prescribes certain disclosure requirements for advertising or promotional material in respect of financial products. The types of advertising and promotional material caught by this provision falls under one of two limbs:

1) Advertisements that advertise a product (under Section 1018A(1)(a)); or

2) Published statements that are reasonably likely to induce people to acquire a product (under Section 1018A(1)(b)).

The intention of the first limb of Section 1018A(1) is to catch all product advertisements (i.e. all advertisements that advertise a particular financial product for acquisition by retail clients) regardless of whether such advertisements are reasonably likely to induce people to acquire the product.

The Act does not define what an "advertisement" is nor does it provide any guidance on whether a particular advertisement "advertises a product". In discussing the application of section 1018A, the Revised Explanatory Memorandum to the Financial Services Reform Bill 2001 suggests that an advertisement must be more than image advertising to be caught under the Act, (refer 14.159).

In respect of such advertising, Section 1018A requires identification of the issuer or the issuer and seller of the product (depending on the distribution channel for that product), an indication that a PDS is available for that product and where it can be obtained, and an indication that a person should consider the PDS in deciding whether to acquire, or to continue to hold, the product.

The combined effect of sub-Regulation 7.7.02 (5A) and Regulation 7.7.20 is to provide a limited exemption from providing a general advice warning and an FSG when financial service providers advertise in the media or on billboards, that is, to the general public.

The explanatory notes accompanying Batch 6 state that providing the general advice information via a medium such as radio presents practical difficulties and involves extra broadcast time and expense. ICA believes this is also the case with Section 1018A disclosure and radio advertisements.

One of the principal disclosure difficulties associated with radio advertisements is the inability to 'super impose' disclosure text over graphics or paper space, as with visual and print media advertisements.

Cost of compliance

Some ICA member companies have attempted to calculate the cost of compliance with Section 1018A disclosure requirements in the context of radio investment. It is calculated that the additional time to be added to current radio scripts in order to comply with the said Section is approximately 15 seconds. (In some scenarios, the disclosure imposed by FSRA may take up more time than the product advertisement itself).

Conservatively, the additional time would equate to an additional cost of approximately $1 million relative to current expenditure of approximately $2 million, that is, the additional cost may be in the vicinity of 50%.

ICA believes that even if broadcast time was not extended and current advertisement content was modified to incorporate Section 1018A disclosure, there is a significant 'opportunity cost' borne by the advertiser in terms of dilution of marketing impact.

The indication from ICA member companies is that they will be forced to consider the prospect of a severe reduction in radio investment and exposure in the event that relief from Section 1018A disclosure requirements is not provided.

Policy considerations

In view of the policy direction indicated by the Batch 6 Regulations, ICA believes that the rationale for the continued application of Section 1018A to general public radio advertisements is somewhat diminished.

The fact is, that in the event a retail client responds to the radio advertisement and contacts the providing entity, that person will receive relevant disclosure, oral and written, at or very soon after that time.

The provision of the relief sought would not affect the level and quality of product information possessed by prospective retail clients.

ICA believes that strict compliance with the regulatory prescription set out in Section 1018A would be disproportionately financially burdensome to those ICA member companies that include radio advertising within their marketing strategy, without any clear concomitant benefit to the prospective retail client. Such disclosure may in fact confuse the prospective retail client.

ICA believes the likelihood and extent of potential consumer detriment resulting from the proposed relief is, as indicated above, minimal. The financial products advertised are subject to adequate regulation and prospective retail clients will retain the protection intended by Parliament.

General insurance products are also subject to the cooling off provisions of Section 1019B and a retail client will always receive a PDS within the cooling-off period if a financial product has been acquired.

Corporations Amendments Regulations (Batch 8)

Dollar disclosure – Proposed amendments to Regulations 7.7.11, 7.7.12, 7.7.13, 7.9.15A, 7.9.19A & B, 7.9.20A & B and 7.9.75

The commentary to the Draft Corporations Amendments Regulations 2004 (Batch 8 – Disclosure in dollar terms) explains that the amendments made by the Senate to the Financial Services Reform Amendment Bill 2003 require the disclosure of items in dollar terms unless otherwise provided in the Regulations. These requirements affect disclosures in the following documents:

- Statements of Advice
- Product Disclosure Statements
- Periodic Statements.

The proposed Amendments are scheduled to commence on 1 July 2004.

A common wording appears in each of the proposed Regulations and refers to:

"If ASIC determines that, for a compelling reason, it is not possible to state the information to be disclosed … as an amount in dollars, the information may be set out as a description of …"

ICA strongly believes these words create potential difficulties for ASIC and general insurers, for example:

- There is no definition of the term "compelling reason"
- There is no guidance as to how ASIC should arrive at its determination or any mechanism for review of ASIC decisions
- It is questionable whether ASIC has the resources to cope with a flood of applications for determinations
- ICA believes the process will involve considerable time and expense without commensurate benefit to consumers
- For many insurance products it is not possible to state the product benefits as dollar amounts in the PDS. For example, any policy that covers a partial loss on an indemnity basis
- For many policies, it is not possible to state the cost of the product as a dollar amount in the PDS because the cost varies according to the sum insured and other rating factors
- While there may not be any difficulty in stating commission for an insurance product as a dollar amount in an SoA, in many cases it is not possible to state other benefits as a dollar amount, because those other benefits do not relate just to the particular product that is the subject of the advice

- ICA believes that the introduction of the term "compelling reason" has the potential to lead to inconsistent decisions being made by ASIC.

ICA recommends an alternative approach, which would involve ASIC conducting spot audits of FSG's, SoA's and PDS's and for ASIC to ask providers to justify the basis where they have failed to disclose in dollar terms. This would be a more effective use of ASIC resources. By combining active high profile surveillance by ASIC, a very strong incentive to comply would be created and allow flexibility for the genuine cases where it is not possible to disclose in dollar terms.

ICA believes the many requirements currently contained in the Corporations Act and Regulations regarding the content of disclosure documents are sufficient to allow ASIC to act where the disclosure of remuneration or cost is not in accordance with the law. ASIC already has powers to direct defective documents be withdrawn and rectified.

ICA believes it is important to note that the proposed Regulations would cut across the position previously agreed by ASIC related to the general insurance industry, which allows the issuer of a PDS to satisfy the requirements of Section 1013D of the Act by setting out the means by which the cost of the product, premium, is calculated. This position was arrived at after considerable debate, discussion and compromise. A reversal of this decision would create unnecessary uncertainty and cost in the preparation of product disclosure documentation by general insurance companies.

ICA's preferred approach is to leave the question of appropriate disclosure to the entity responsible for the disclosure document, the product issuer or licensee.