
Policyholder Protection

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Key developments in 2010/11

Key development Summary of issue

The Future of Financial Advice Reforms

On 26 April 2010, the Federal Government's proposals regarding the provision of financial advice were announced, to improve trust and confidence in the financial planning sector. The Government's Future of Financial Advice (FoFA) reforms are designed to tackle the conflicts of interest that may have threatened the quality of financial advice provided to investors, leading to the mis-selling of financial products that culminated in the high profile corporate collapses of Storm Financial, Opes Prime and MFS.

The FoFA reforms represent the Government's response to the recommendations from the 2009 Ripoll Inquiry into financial products and services in Australia.

The FoFA package includes:

- A proposed **ban on conflicted remuneration structures** regarding the distribution and provision of advice for retail investment products including managed investments, superannuation and margin loans. This includes commissions and volume based payments in relation to these products.

Commissions on risk insurance both within group and individual superannuation will be banned from 1 July 2013.
- A proposed introduction of a **statutory fiduciary duty** for advisors towards their clients. The duty will oblige advisers to act in the best interests of their clients and to place these ahead of their own when providing personal advice to retail clients subject to a 'reasonable steps' qualification.
- A proposed introduction of '**Advisor charging**' disclosure requirements to improve the transparency and flexibility of payments for financial advice. Advisers will be required to agree their fees directly with clients and disclose the charging structure to clients in a transparent manner. A renewal notice will also be introduced where the adviser is required to send a bi-annual notice to the client when providing ongoing service, where if the client opts out, the adviser will not be able to continue charging the client.

The legislation to implement the majority of the FoFA reforms, including the prospective ban on conflicted remuneration structures, statutory fiduciary duty and adviser charging regime will commence from 1 July 2012.

Key development *Summary of issue*

Privacy law

On 24 June 2010 the Senate referred the *Exposure Drafts of Australian Privacy Amendment Legislation* to the Senate Finance and Public Administration Legislation Committee (the Committee) for inquiry and report by 1 July 2011.

The exposure draft consists of 2 parts:

Part 1 – Australian Privacy Principles

The exposure draft of the new Australian Privacy Principles (APP) will form a key part of the proposed amendments to the Privacy Act, replacing the current Information Privacy Principles (for the Commonwealth public sector) and the National Privacy Principles (for the private sector).

There are 13 new Principles set out in the exposure draft which address how organisations collect, retain and disclose personal information.

Further reforms to the Privacy Act will be released for public consultation in stages.

Part 2 – Credit Reporting

In January 2011, draft comprehensive credit reporting provisions were provided to the Committee for review and tabling.

This exposure draft contains new provisions relating to collection, use and disclosure of credit reporting information and aims to simplify existing laws. The new scheme will be underpinned by a new industry-agreed Credit Reporting Code of Conduct (the Code) which will be subject to approval by the Australian Information Commissioner.

Public submissions on the topic concluded in late March 2011, with tabling date yet to be advised at the time of this publication.

Key development **Summary of issue**

Other Regulator and Government developments

In the last 12 months, there have been a number of regulatory and legislative developments which may affect the insurance industry from a policyholder protection perspective.

These include:

- **APRA Life and General Insurance Capital project** – the Australian Prudential Regulation Authority (APRA) provided a brief industry update in December 2010 on its insurance capital project (LAGIC). Refer to Chapter 1 for detail.
 - **Basel minimum capital requirements** – APRA announced in January 2011 that the Basel Committee on Banking Supervision issued minimum requirements to ensure that all classes of capital instruments fully absorb losses at the point of non-viability before taxpayers are exposed to loss. APRA has also advised general insurers that aspects of these reforms will be considered by APRA in its general insurance capital requirements.
 - **ASIC Compensation and Insurance Arrangements** – The Australian Securities and Investments Commission (ASIC) released an updated version of Regulatory Guide 126 Compensation and Insurance Arrangements for Australian Financial Services licensees in January 2011. The update sets out ASIC's policy on the mandatory compensation requirements for AFS licensees, including minimum requirements for adequate professional indemnity insurance.
 - **Definition of 'flood' insurance** – A standard definition of 'flood' for the purpose of flood insurance has been determined by the Government, in close consultation with the Insurance Council of Australia and consumer groups in April 2011. Other natural disaster questions are being examined by the Natural Disasters Insurance Review, which is due to report back to the Government by 30 September 2011. The inquiry looks into the availability and affordability of insurance for flood and other natural disasters.
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Regulatory Framework for the Insurance Industry

The Australian regulatory framework is designed to provide comprehensive supervision over the insurance industry and effective customer protection through the following elements:

- Solvency of insurance providers – maintaining a competitive and viable insurance industry within Australia
- Policyholder protection – protecting the overall interests of policyholders through product disclosure, insurance business requirements and contracts
- Sales practice regulation – providing sales advice and customer service of the highest possible standard
- Ability to pay claims – maintaining sufficient capital and resources to pay claims as they fall due
- Sources of redress – offering adequate sources of redress in the event of policyholder dissatisfaction.

The framework is administered by the Australian Prudential Regulation Authority (APRA), the Australian Securities and Investments Commissions (ASIC) and the Australian Competition and Consumer Commission (ACCC). The Insurance Council of Australia has also developed an Industry Code of Practice which aims to:

- to promote better, more informed relations between insurers and their customers;
- to improve customer confidence in the general insurance industry;
- to provide better mechanisms for the resolution of complaints and disputes between insurers and their customers; and
- to commit insurers and the professionals they rely upon to high standards of customer service.

An outline of the areas of regulatory supervision, responsible regulatory authority and corresponding Commonwealth legislation is outlined in the following table.

Table 6.1 – Policyholder protection – An overview

		Commonwealth Legislation										Industry Supervision		
		Corporations Act	Life Act	Insurance Act	Insurance Contracts Act	Trade Practices Act	Price Surveillance Act	Privacy Act	Financial Services Reform Act	National Health Act	Lifetime Health Cover	Medical Indemnity Act	General Code of Practice of Practice	
	Regulatory Body	Licence requirements	APRA	APRA	ASIC	ACCC/ ASIC	ACCC	Privacy Commissioner	ASIC	PHIAC	PHIO	PHIAC	Medicare Australia / APPA	FOS
Pre Sale	Product and Insurance Business/ contracts	✓	✓	✓	✓				✓	✓	✓		✓	
	Pricing and competition					✓	✓					✓		
Sale	Sales practice regulation					✓		✓	✓				✓	
	Ability to pay claims	✓	✓	✓						✓		✓		
Claim	Sources of redress							✓	✓	✓				✓
	Use of personal information							✓						

Product disclosure, insurance business and insurance contracts

Consumers need clear and relevant product information that is directly comparable to information on other products in the insurance market. The Corporations Act requires insurers to give product documentation to consumers before they purchase an insurance product. Product disclosure documentation includes the provision of a Financial Services Guide (FSG), the Statement of Advice (SoA) and the Product Disclosure Statement (PDS).

In addition to the standard product disclosure documentation, the Insurance Contracts Act places the following requirements on general insurers:

- detailed information pertaining to policy and claim limitations and disclosures must be provided to policy holders;
- when renewing policies, the insured has a duty of disclosure as to matters that would increase the risk of the insurer;
- the insurer must advise the intention and rate of renewal at least 14 days prior to expiry of existing policy, otherwise the policy is automatically renewed with no premium;
- an unpaid instalment can prevent claim payment only if this is made clear to the insured and it is overdue by at least 14 days;
- the insured must be informed if liability cover is on a claims-made basis; and
- insurers must disclose averaging provisions clearly and in writing.

Sales practice regulation

The Corporations Act aims to ensure policy holders receive quality sales advice and service by requiring advisers to possess appropriate skills and knowledge and adhere to prescribed conduct and disclosure standards.

In order to demonstrate that sales representatives have appropriate skills and knowledge, insurers are required to:

- have documented procedures to monitor and supervise the activities of representatives to ensure they comply with financial services laws;
- ensure all representatives who provide financial services are competent to provide those services as outlined in ASIC's Regulatory Guide 146;
- meet ongoing educational requirements;
- maintain records of all training undertaken; and
- ensure "responsible officers" meet ASIC standards for knowledge and skills.

Insurance providers must also adhere to the following procedural requirements as part of their sales practices:

- Confirm, electronically or in writing, the issue, renewal, redemption or variation of policies within a reasonable time frame.
- Offer a 14-day "cooling-off" period during which customers have the right of return. For risk insurance products, the amount refunded can be reduced in proportion to the period that has passed before the right of return is exercised.
- Consumers must be given the option to register a "no contact, no call" request, similar to marketing consents required under the Privacy Act 1988.

6.5

Ability to pay claims

The Financial Claims Scheme (FCS) enables eligible general insurance policy holders to claim under a dedicated compensation scheme for valid claims against a failed general insurer, instead of having to pursue claims in the normal liquidation process. Eligible general insurance policyholders are individuals insured with an APRA-regulated general insurer, small businesses (annual turnover less than \$2million) and not-for-profit organisations. The FCS also allows the appointment of judicial managers to failing general insurers with powers to advance the interests of policy holders and the stability of the financial system.

6.6

Sources of redress

The Corporations Act requires all insurance companies to have clearly documented internal dispute resolution procedures for retail clients, and to belong to an external dispute resolution scheme which meets ASIC-approved standards. Health insurance complaints are handled by the Private Health Insurance Ombudsman (PHIO), as authorised by the Government. It also deals with complaints from health funds, private hospitals or medical practitioners regarding health insurance arrangements.