



ASIC

Australian Securities & Investments Commission

Regulatory update to the general insurance industry

*A speech by Greg Medcraft, Chairman,
Australian Securities and Investments Commission*

*Insurance Council of Australia Annual Forum (Sydney, Australia)
17 February 2017*

CHECK AGAINST DELIVERY

Introduction

Thank you to the Insurance Council of Australia for inviting me to be here.

I have three main topics I would like to talk about today. First, I want to talk about the environment that we are currently in – and the opportunities that I think this provides for the general insurance industry. Second, I will talk about what ASIC has been doing in insurance – and where we are going over the next year. Third, in bringing together my previous comments, I would like to end by talking about the importance of having a good culture.

The current environment

You might agree that 2016 was an eventful year for the insurance industry. There has been an increased public, media and government focus on insurance, as well as progress on important law reforms in this space. Customer expectations have changed, and customers are more empowered than ever. We now live in a world with technology and social media at our fingertips. Individuals now have unprecedented access to information and, as a result, if businesses are not behaving in the right way, the crowd will let them know, if not the headlines. And of course we have seen the conduct of financial institutions – including insurers – often adversely highlighted by the media.

Responding to these changing community expectations, the Government is increasingly calling for, and looking at, ways to foster conduct that customers can have trust and confidence in.

This has seen the commencement of a PJC Inquiry into life insurance last year, which will continue in 2017. And it is unlikely that interest will be limited to life insurance, with a Senate Committee Inquiry into general insurance commencing this year.

Against this backdrop, we are in a significant time of law reform.

We are seeing the important recommendations of the Financial System Inquiry progress. Of particular relevance to your industry are:

- the product intervention power
- the product governance obligation
- the review of ASIC's enforcement regime, including penalties.

The Government has committed to accelerating the implementation of this law reform and I will talk about this more later.

In addition, ASIC has been working with Government and other regulators as part of the review of the Australian Consumer Law, particularly on the proposed extension of unfair contract term protections to insurance contracts.

The Government has also asked Treasury to consult on the recommendation made in our claims handling report¹ that the exemption of insurance claims handling from the financial services conduct provisions of the Corporations Law be removed.

In the current environment, I think there is a unique opportunity for the industry to work with Government and regulators – as well as consumers – to bring about positive change, to make sure consumers are getting the products they need, and that they can have trust and confidence in the firms they deal with.

ASIC's insurance work in 2016 and looking forward

Our work in 2016

I will now talk about some of the work that ASIC has undertaken over the last year in insurance, which will continue to be a focus throughout 2017. While there are many topics I could touch on that might be relevant, today I will focus on two key pieces of work:

- ASIC's review of life insurance claims handling, and
- our continuing work on add-on insurance.

¹ [Report 498](#) *Life insurance claims: An industry review* (REP 498)

Before I touch on these, I might first mention, as you probably know, that in April last year the Government committed to a \$127 million reform package. This includes providing \$61 million to enhance ASIC's data analytics capabilities and data management systems. It also includes \$57 million to enable increased surveillance and enforcement in key areas of risk, including areas of relevance to your industry: insurance and breach reporting. These measures will further strengthen our ability to proactively detect, understand and respond to misconduct.

Claims handling review

In October last year, ASIC released its findings following an industry review of life insurance claims handling practices. While the review was specific to life insurance, a number of findings, recommendations and follow up work are relevant to general insurers. Issues such as consumer understanding of coverage, concerns about whether claim denials are fair, and effective dispute resolution, are common across life and general insurance.

Today, I would like to highlight one area in particular: our review found a clear need for better quality, more transparent and more consistent data on life insurance claims.

ASIC and APRA are currently working jointly on an initiative to establish a consistent public reporting regime for life insurance claims data and claims outcomes on an industry and individual insurer basis.

We acknowledge that some public reporting for the general insurance sector exists in the form of the Code Governance Committee's annual public reports. However, as the life insurance data framework develops, general insurers should continue to look for ways to improve their own reporting frameworks to keep up to date with evolving standards, particularly around consistency and comparability. As part of this process, we will consult with industry and consumer groups to discuss common data definitions and the need for life insurers to update systems to enable consistent and reliable reporting.

ASIC's claims handling review was in part prompted by concerns from the public, media and Government. And it is important that the general insurance industry does not consider itself immune to this type of scrutiny.

The focus on life insurance during 2016 is an important reminder of the 'front page test' and the need for industry to focus on putting the customer at the centre of their business.

Add-on insurance

As with our claims handling review, ASIC's initial work on add-on insurance was focused on the life insurance industry. This time last year, ASIC's review of general insurance add-ons sold through car dealers was not yet complete, however we already had concerns about claims ratios which were less than 10 cents in the dollar.

At this forum last year, ASIC's Deputy Chairman Peter Kell made clear that 2016 would be a year for engaging with the general insurance industry about the poor consumer

outcomes in the add-on market. He also made clear that if our concerns about add-on insurance continued in 2017, our strategy would become more enforcement focused.

Since then, ASIC has completed its review of general insurance add-ons sold through car dealers. Many of you would be aware of the findings of ASIC's report,² including:

- an overall claims ratio of 9% across the five products we reviewed
- car dealers receiving four times more in commission payments than consumers received in claims, with commissions paid as high as 79%
- a sales environment that inhibits good decision making about the product because of conflicts of interest and pressure sales.

These findings are, to put it bluntly, shocking.

Insurers have designed complex and extremely poor value products, and put their reputations at risk. And some of the most vulnerable consumers in society are paying the price.

A couple of interesting questions for those here today are: Have you or your colleagues purchased these particular add-on products? Do you recommend all of these products to your friends and family on a regular basis?

The general insurance industry has put forward a range of proposals to address ASIC's concerns. We are pleased to see industry engaging on these issues, but overall the proposals fall short of addressing the underlying issues in this space.

So you shouldn't be surprised to hear me say that our work on add-on insurance continues, and we will look to use our full range of powers to seek better consumer outcomes. This includes work that we have already commenced or are currently considering, including:

- introducing a deferred sales model
- raising training standards for add-on general insurance products which are complex and poorly understood by consumers
- holding insurers to account to deliver products that are designed with consumers' genuine needs in mind and offer good value
- enforcement action against individual insurers who have breached the law
- public reporting on individual insurer outcomes and key value measures for consumers.

We will use our full regulatory toolkit – including using our modification powers in the Corporations Act – to respond to poor consumer outcomes in this sub-sector.

² [Report 492](#) *A market that is failing consumers: The sale of add-on insurance through car dealers* (REP 492)

The year ahead in insurance

ASIC's additional funding from Government will allow us not only to take more proactive steps to assess the current issues, but also allow us to look back at previous work we've conducted, to ensure industry has taken action to address our concerns.

As set out in ASIC's corporate plan, we are also focused on incorporating culture and incentives into our risk-based surveillances. Where we see poor culture, this is a red flag that indicates there may be misconduct in a firm and we will dig deeper.

No-claim discounts health check

This focus on culture will guide us as we look at practices such as the promotion of no-claim discount schemes by insurers.

No-claim discount schemes are usually promoted to consumers as 'rewarding safe drivers'. However, our report published in 2015³ found that, for example, making a 'not-at-fault claim' can have an effect on the underlying premium even where there is no effect on the no-claim discount rating.

Our report made clear that insurers who choose to retain such schemes must implement measures that meaningfully improve consumers' understanding of how they work. In 2017, we will be finalising a follow-up review of the industry to ensure insurers are complying with their obligations to provide consumers with accurate information.

I strongly encourage insurers to carefully review the operation and disclosure of their respective schemes in light of our report.

Surveillance and investigation practices

We are also planning to review surveillance and investigation processes used by insurers to identify fraudulent claims. This is an area that has been highlighted by consumer representatives and media who have raised concerns about processes which are detrimental to consumers. Industry has been on notice of these concerns, and has had time to review them and address any shortcomings.

Law reform

As I mentioned earlier, there are a number of key reforms underway that will have significant impacts for both industry and ASIC.

In December, the Government began consultation on the introduction of a new product design and distribution framework for financial products, and a product intervention power which will enable ASIC to take direct action to deal with significant shortcomings in products or conduct that result in consumer detriment.

³ [Report 424](#) *Review of no-claims discount schemes* (REP 424)

Product design and distribution

The product design and distribution obligations will mean that issuers of financial products – including general insurers – will be obliged to:

- identify an appropriate target market for their products
- consider whether the product meets the needs of those individuals and is capable of being understood by them
- select distribution channels that are likely to deliver the products into the hands of individuals in the target market.

On the face of it, you might expect that this should not mean significant change for industry. These look to be sound principles that one would expect a well-run business, looking to treat their customers well, would follow. And yet, our work on add-on insurance highlights the need for these obligations. Our findings put beyond any doubt that many of the disciplines that the new obligations will introduce are still needed – not just in one firm, but across the market.

Product design and distribution that puts good consumer outcomes front and centre should be at the heart of any insurers' business.

Product intervention power

This brings me to the product intervention power. The new power envisages ASIC being able to take action in relation to product features, the types of consumers who can access a product, and the circumstances in which they can do so. This would be warranted where significant consumer detriment has been identified.

In a world of effective design and distribution, there should be no need for such an intervention. But it does mean that where other avenues have been exhausted and conduct that significantly damages consumers' interests persists, ASIC will be able to act more swiftly.

However, I want to make it clear to you all that ASIC is not waiting for these additional powers before acting to address problems that we see today.

Penalties

We have also recommended more significant penalties for misconduct relating to insurance claims handling, which will be reviewed as part of Government's review of ASIC's enforcement powers. This will help strengthen the regulatory framework for claims handling, and improve ASIC's ability to take action where we identify concerning conduct.

The public expects nothing less.

Why culture matters

I want to comment finally today to you, that culture matters. At the centre of everything I have talked about today is a firm's culture.

Good culture is good for the bottom line and it is critical for firms that want to be around for the long term. Many studies have found that good culture is good for business and generating long-term shareholder value.

There are a number of ways that having a good culture can benefit your organisation. For example:

- increasing customer loyalty, brand and reputation
- reducing or avoiding the financial impact of fines or remediation
- attracting and retaining staff.

Poor culture, on the other hand, can lead to misconduct and result in significant financial costs, including the cost of remediation, compensation and fines; as well as not necessarily attracting and retaining high performing staff.

And, in talking about culture, I can't help but come back to the add-on insurance products that we've highlighted in our reports. A culture that focuses on commissions and conflicted remuneration for intermediaries over and above providing consumers with a product that meets their needs is not sustainable. A culture where it is acceptable to simply pass a product on to a third party, with no consideration for who the final consumer might be and whether the product offers them any value at all, will inevitably lead to poor consumer outcomes.

Culture should also be at the forefront of the general insurance industry's mind as you endeavour to review the industry's code of practice this year.

This forum is an opportunity for you to think about the cultural foundation you want this industry to be built on in the future.

Conclusion

I do hope this gives you a sense that the insurance market continues to be at the forefront of much of ASIC's regulatory agenda.

We hope to continue to work collaboratively with your industry in the coming year to help ensure that consumers can have trust and confidence in the insurance industry.