**Royal Commission into Misconduct in the Banking,**

**Superannuation and Financial Services Industry**

**Policy Questions arising from Module 6**

## 1. Introduction

1.1 To provide context to my submission in respect of Policy Questions arising from Module 6 of the above Royal Commission, a short background to my involvement in the Life Insurance industry is as follows:

1.2 I have worked in the Life and Disability Insurance industry globally for 47 years. In that period of time I have spent approximately 41 years working in the disciplines of underwriting and claims.

1.3 My work has involved business in over 55 countries around the world including Australia. In the past 16 years I have been based in Australia and my most recent employment is as a consultant advising Australian Life Insurance companies on Life Insurance risk management issues, particularly in the field of underwriting and claims.

1.4 I am qualified as a Fellow of the Chartered Insurance Institute by examination and have a Diploma in Medical Underwriting awarded by the Assurance Medical Society in the UK for which I gained a distinction in the examination. I also hold the honorary qualification of a Fellow of the Assurance Medical Society, which was awarded to me for my contribution to insurance medicine. I am a Fellow & Life Member of the Australasian Life Underwriting and Claims Association.

1.5 Specifically in respect of this submission, my consultancy projects have involved advising Australian Insurers on practical approaches to Life & Disability Insurance underwriting and claims. I have been involved in projects to review complex Life & Disability Insurance claims decisions and I am an independent member of one company's claims review committee.

2. **Policy Question – Section E Claims Handling – 19 & 20 *Should life insurers be prevented from denying claims based on the existence of a pre-existing condition that is unrelated to the condition that is the basis for the claim? Should life insurers who seek out medical information for claims handling purposes be required to limit that information to information that is relevant to the claimed condition?***

2.1 I am responding on Policy Questions 19 & 20 together since they are linked in that if an insurer was prevented from considering a matter in the life insured's history that was not related to the condition which was the basis of a claim then one would assume there would be no need to ask for information that was not relevant to the claimed condition.

2.2 It is my experience in reviewing claims that there is not a systemic issue of insurers searching for information simply in order to decline claims. However, the Royal Commission appears to have identified some occasions when this has happened. It is my opinion any such action proven to be taken by insurers in these cases is not ethical, goes against community standards and expectations and should not be allowed to happen.

2.3 However, I do believe that an insurer, when presented with information that should have been disclosed at the underwriting stage, has a responsibility towards its existing and future lives insured to ensure that an equitable approach is taken to all. In this respect the issue is the principle of equity or fairness with each individual paying for the known risk that they bring to the fund.

2.4 If we are to expect an individual who carries a known extra morbidity or mortality risk to disclose such a risk at the application stage and pay the appropriate extra premium for that risk then it is inequitable that an individual who fails to disclose the extra risk should be granted insurance without any extra premium to pay and then benefit from that insurance.

2.5 Not raising an issue at the claims stage regarding such non-disclosure or misrepresentation has the potential to allow such inequity to happen and the extra cost that has not been paid by the individual who does not fully disclose being borne by other lives insured.

2.6 In addition, if when presented with such information an insurer does not take action and then at a later stage, perhaps when the insured is claiming for a condition that does directly relate to the non-disclosed condition, the insurer is likely to be seen both legally and from community expectations to have foregone the opportunity to take any action at this later stage in view of the fact that no action was taken earlier. This I suggest would arise from the fact that an insurer was aware of a non-disclosed issue and continued to collect premiums without taking any action regarding the non-disclosure.

2.7 Whilst theoretically, the insurer might be prevented from seeking such additional information at the original claim stage, the practicalities are that doctor's referral reports to specialists will often detail all the medical history and not just focus on the referred issue in isolation.

2.8 In addition, a claimant who knew medical information was being collected might assume that the insurer had access to all medical detail and then be upset if an issue regarding non-disclosure was raised at a later date.

2.9 In my opinion, in addition to the question of equity and the practical considerations regarding the collection of limited information, there must be some encouragement for applicants to disclose fully. That encouragement is that if an individual does not disclose they run the risk of their policy being void. This principle is also described in Insurance Contracts Act 1984 as amended (ICA) which states in Section 31 that a court when exercising the power to disregard avoidance "...shall have regard to the need to deter fraudulent conduct in relation to insurance..." .

2.10 Therefore if one accepts the principle of the insured's duty of disclosure as outlined in Section 21 of the ICA then it follows that an insurer has an obligation to take the appropriate action on discovering any non-disclosure or misrepresentation and therefore has a right to seek any medical information that would have been relevant to the decision of the insurer, irrespective of the cause of claim.

2.11 The fundamental issue that is raised in the Policy Questions 19 & 20 is *if the matter not disclosed is unrelated to the cause of claim then why should an insurer be able to take any action*. To answer this question one has to understand one of the principles of Life Insurance underwriting.

2.12 This principle can be best explained using a simple example: 100 individuals are suffering from a medical condition that statistically gives rise to an **extra** risk of claiming (above and beyond the standard risk on which the premiums are based) due to the fact that a certain number of the individuals in this group will develop a worsening disease and claim. The insurer does not know which individuals will suffer this consequence but can statistically quantify the **extra** risk for the group as a whole. The insurer then charges each member of the group an extra premium which equates to the total extra risk divided by, in this example, 100 in the knowledge that these extra premiums combined will pay for the extra number of claims. The insurer expects that some individuals will go longer without the need to claim and some will claim earlier but charging each member of the group the relevant extra premium means that the cost of the risk is covered and shared equitably amongst the particular population who present with this extra risk. Therefore, if an individual claiming for a separate matter also carries this extra risk then it is irrelevant that the extra risk is not the cause of claim as they have been provided with cover for the extra risk and, in

accordance with the principle of equity, should share in the burden of the cost of that extra risk rather than let that burden be borne by the other lives insured.

2.13 If one member of the population fails to disclose their known extra risk then instead of the extra cost being shared by the 100 members of the group it is borne by the whole portfolio with an extra cost to all. Whilst this extra cost might not be immediately apparent, ultimately it would show in the actuarial experience which would lead to a rise in premiums for all lives insured whether in this particular group or not.

2.14 Therefore the principle of equity dictates that all known risks should be disclosed and paid for and if not there must be remedies.

2.15 If this principle of equity between lives insured is accepted then one should ask how can the principle be enforced **fairly** and what protections are there for lives insured when such a principle is enforced.

2.16 Section 21 of the ICA sets out what an individual is required to disclose. There are a number of safeguards for lives insured in this section e.g. it must be a matter that the insured knows to be relevant to the insurer's decision and one that a reasonable person could be expected to so know. This provides some protection against a life insured being taken to task on a matter that they honestly believed to be irrelevant.

2.17 Under Section 29 of the ICA the remedies available to an insurer in the case of non-disclosure or misrepresentation are set-out in detail and also contain some safeguards for the life insured.

2.18 An insurer cannot take any action if they would have entered the contract on the same terms even if the matter had been fully disclosed. Therefore the matter must be relevant to the decision of the insurer.

2.19 An insurer can only avoid a contract for non-fraudulent non-disclosure or misrepresentation within the first 3 years. After this the insurer has to prove fraud which is a much higher bar to reach. This provides some protection for those lives insured who have held a policy for some years.

2.20 The insurer, as an alternative to avoiding the policy, has the right to vary the contract to place the insurer in the same position as if the matter had been disclosed. However, the insurer can only vary the contract to the degree that it is not inconsistent with the position other reasonable and prudent insurers would have taken. I believe more insurers will take this approach where possible as it is in the interest of the insurer to keep the policy on the books and also in the interest of the life insured as cover would continue albeit on the correct basis.

2.21 Furthermore Section 31 of the ICA allows a court to disregard avoidance in certain circumstances, particularly if it would be harsh not to do so. Again a further protection for the life insured.

2.22 Therefore, I do believe that there are some protections already in place for insureds and these protections could be applied by courts or by External Dispute

Resolution Providers such as the Australian Financial Complaints Authority or even by the regulator if it was given these powers.

## 3. Conclusion

In conclusion, I respectfully submit that to prevent insurers from denying claims based on the existence of a pre-existing condition that is unrelated to the condition that is the basis for the claim and to limit the obtaining of information that is relevant to the claimed condition goes against the principle of equity on which the whole insurance concept is based. In addition, to do this would ultimately penalise those policyholders who have been honest in their disclosures and would therefore be inequitable. Also the practical issues have the potential to lead to problems later in the course of the policy.

I agree it is essential that policyholders are protected from unreasonable denial of claim and I believe that there are enough safeguards in the ICA, provided they are applied diligently, to prevent such activity.

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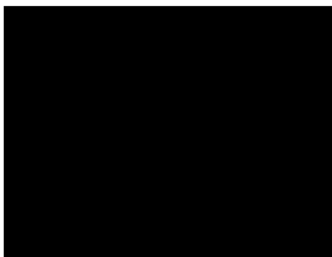

**11 October 2018**