Royal Commission into Misconduct in the Banking,
Superannuation and Financial Services Industry

SUBMISSIONS BY ANZ IN RESPECT OF GENERAL QUESTIONS - ROUND 6 HEARINGS

1. This submission responds on behalf of Australia and New Zealand Banking Group Limited and its associated entities, including OnePath Life Limited (**OPL**) or OnePath General Insurance Limited (**OPGI**) (collectively, **ANZ**) to Counsel Assisting's Round 6 Policy Questions.

Question 1

Is the current regulatory regime adequate to minimise consumer detriment? If the current regulatory regime is not adequate to achieve that purpose, what should be changed?

2. ANZ considers that the current regulatory regime[1] is generally adequate to minimise consumer detriment but notes that the following reforms, if implemented, will adjust its form and effectiveness in a positive way:

   (a) the Treasury Laws Amendment (Design and Distribution Obligations and Product Intervention Powers) Bill 2018 (Cth) (the **Bill**) currently before the Commonwealth Parliament;

   (b) the pending version of the Life Insurance Code of Practice (**LICOP**);

   (c) the Unfair Contract Terms (**UCT**) reform of the kind set out in response to question 29, below;

   (d) the reforms to section 912A of the *Corporations Act 2001* (Cth) (**Corporations Act**) of the kind set out in response to questions 17 and 18, below;

   (e) the reforms recommended by the ASIC Enforcement Review Taskforce Report; and

   (f) changes to disclosure of the kind identified in the response to question 4, below.

[1] Including the changes to life insurance remuneration introduced by the *Corporations Amendment (Life Insurance Remuneration Arrangements) Act 2017* (Cth).

A. PRODUCT DESIGN

Question 2

Are there particular products – like accidental death and accidental injury products – which should not be sold?

3. ANZ responds to this question on the basis of stand-alone accidental death and accidental injury products (collectively, **accident products**) rather than like benefits provided as part of a broader life policy.

4. ANZ acknowledges the evidence adduced before the Commission and ASIC's findings in Report 587 about issues relating to accident products. ANZ has suspended the sale of its accidental death insurance pending further review of the design, pricing and distribution of this product.

5. It remains the case, however, that Australian consumers face a range of personal risk exposures, including accidents occasioning injury or death, against which they might reasonably wish to insure themselves by way of stand-alone accident products. For example, accidental death insurance can be a suitable offering for customers who have been denied life cover on medical grounds. In other cases, a customer may wish to add an accident product to top up existing life cover in superannuation, or because they want to insure against accidental death or injury, but not against illness.

6. So long as there is demand for accident products, the industry should be permitted to meet it, subject to consumer safeguards. Poor sales practices by certain insurers should not be allowed to detract from the reality that customers may obtain good value from these products when they are distributed appropriately.

7. Concerns about the value of accident products are best addressed by ensuring that:

   (a) such products are designed and distributed in a manner cognisant of the needs and circumstances of the target market (as discussed in response to question 4, below); and

   (b) product disclosure promotes customer understanding (including in respect of existing customers).

8. The Bill would, if passed, represent a significant step towards ensuring the appropriateness of accident products.

9. The design and distribution obligations (**DDO**) would require insurers to consider whether an insurance product is likely to be consistent with the expected financial situation, objectives and needs of a defined target market and to select distribution channels that are reasonably likely to result in the product being sold to individuals within that market. Similar obligations are imposed on distributors.

10. The product intervention power (**PIP**) would provide a further safeguard by allowing ASIC to intervene in circumstances where, despite the above, a product is inappropriately targeted and sold and there is a risk of significant consumer detriment. These powers would enable ASIC to order that a person not engage in specified conduct in relation to the product (including conditionally).

11. In submissions to the Treasury in response to consultations on the DDO and PIP, ANZ has supported the introduction of the measures, with observations made on the then proposed drafting of the Bill.

Question 3

Should the requirements of the Life Insurance Code of Practice in relation to updating medical definitions be extended to products other than on-sale products?

12. Clause 3.2 of LICOP requires that medical definitions in on-sale products be *reviewed* every three years and *updated as necessary* following consultation with relevant medical specialists to ensure that definitions remain current.

13. ANZ supports the regular review of medical definitions in products other than on-sale products (otherwise known as **legacy products**). Consistent with this, since June 2016, medical definitions in OPL legacy products, like its on-sale products, are generally reviewed as part of the annual product review process. Further, where a medical definition in an on-sale product is updated, consideration is given to whether the update can apply to equivalent definitions in legacy products.[2]

14. In principle, ANZ agrees that updates to medical definitions in legacy products should be introduced 'as necessary', recognising that an insurer's ability to introduce such updates is dependent on a range of factors, including pricing and legal restrictions. For example, an updated diagnostic definition of a particular condition, if carried over to a trauma policy, might result in an increased incidence of payouts. This might mean that the update can only be implemented with a price increase to maintain product sustainability – including to ensure that the insurer can continue to meet its obligations and pay claims decades after policies are taken up.

15. While these challenges exist in relation to on-sale policies, they are more acute where legacy products are concerned by reason of the guaranteed renewable nature of these policies and the restriction on unilateral changes unless they are for the benefit of the insured.[3] It follows that, even where an insurer considers it 'necessary' to update a medical definition in its on-sale policies it may not be at liberty to unilaterally introduce a corresponding update in its legacy products if that change would result in a price increase or if the updated definition would be less advantageous to the customer. Any extension of

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2 Statement of Gerard Francis Kerr dated 23 August 2018 (Rubric 6-18) at [32]-[33] (ANZ.999.021.0001 at .0010).

3 See *Life Insurance Act 1995* (Cth) s 9A.

the obligation under clause 3.2 of LICOP to cover legacy products would need to be drafted with these limitations in mind.

16. Where an update to a medical definition cannot be passed back to a legacy product, affected customers have the option to apply for an on-sale policy that incorporates the updated definition, although ANZ recognises that some customers may not be able to access such cover (at all, or on terms otherwise the same as their cover under the legacy product).

B. DISCLOSURE

Question 4

Is the current disclosure regime for financial products set out in Chapter 7 of the Corporations Act 2001 (Cth) and Division 4 of Part IV of the Insurance Contracts Act 1984 (Cth) adequately serving the interests of consumers? If not, why not, and how should it be changed? In answering these questions, address the following matters:

4.1 the purpose(s) that the product disclosure regime should serve;

4.2 whether the current regime meets that purpose or those purposes; and

4.3 how financial services entities could disclose information about financial products in a way that better serves the interests of consumers.

(Despite the reference to the Insurance Contracts Act 1984 (Cth), this question is not limited in scope to contracts of insurance.)

17. ANZ does not presently provide insurance of a kind to which Part IV of Division 4 of the *Insurance Contracts Act 1984* (Cth) (**ICA**) applies. Its observations in relation to this issue are therefore based on experience with the *Corporations Act 2001* (Cth) (**Corporations Act**) disclosure regime.

18. Disclosure regimes should assist consumers to assess the attributes of products against their circumstances and needs to make an informed choice about whether to take out an insurance policy at all or at the price or premium offered by the insurer.

19. A disclosure regime is set out in Part 7.9 of Chapter 7 of the Corporations Act. The effectiveness of this type of regime is contingent on the clarity with which relevant product attributes are presented and consumers' ability to comprehend the potential utility of those attributes to them. Too much disclosure (either in compliance with the law or due to excessive transparency), coupled with the inherent complexity of certain financial products, may militate against clarity.

20. ANZ considers that the current disclosure regime strikes a reasonable balance, but requires periodic review in light of changes in technology and related aspects of the

regulatory architecture.[4] Reforms to the disclosure regime itself may play an important role but are not the only way to improve consumer outcomes. Other initiatives to improve or supplement disclosure include:

(a) measures to improve the availability and accessibility of disclosure documents, such as the use of innovative, digital disclosure as contemplated by ASIC Regulatory Guide 221;

(b) programs that seek to enhance levels of financial literacy among consumers;

(c) measures to ensure that products are designed for, and marketed to, appropriate target groups of consumers or address failures in that regard, including the proposed DDO, PIP[5] and directions power;[6] and

(d) in future, technology which assists consumers to assess whether, based on their historical financial data, the product is likely to be suitable for them and to compare products in a more comprehensive way.

Question 5

Is the standard cover regime in Division 1 of Part V of the Insurance Contracts Act 1984 (Cth) achieving its purpose? If not, why not, and how should it be changed?

21. Division 1 of Part V of the ICA provides a means by which certain minimum contract terms can be mandated for particular insurance contract types. The *Insurance Contracts Regulations 2017* (Cth) (the **Regulations**) set out minimum terms and amounts.[7] ANZ considers that those provisions have been effective in setting minimum standards relating to concepts of 'minimum amount', 'prescribed contract' and 'prescribed event' for various types of insurance contracts and requiring insurers to clearly inform the insured in writing before the relevant insurance contract is entered into if the terms of the contract depart from those minimum standards.[8]

22. The Regulations were updated and enacted in 2017. ANZ considers that their operation is well understood and appropriate in the marketplace. For the reasons explained in response to question 6, it does not consider that an expanded use of the standard cover regime is necessary.

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4 The regime has been subject to iterative review and change over time. See for example *Financial Services Reform Act* 2001 (Cth), *Financial Services Reform Amendment Act 2003* (Cth), and *Corporations Legislation Amendment (Simpler Regulatory System) Act 2007* (Cth)

5 Treasury Laws Amendment (Design and Distribution Obligations and Product Intervention Powers) Bill 2018 (Cth).

6 The Treasury, *ASIC Enforcement Review: Taskforce Report,* December 2017, chapter 8.

7 Minimum coverage and amounts are set out in the Regulations, in relation to: motor vehicles (r 15 – 17); home buildings insurance (r 18 – 20); home insurance (r 21 – 23), sickness and accident insurance (r 24 – 26); consumer credit insurance (r 27 – 26); travel insurance, (r 30 – 32); flood related insurance. The minimum coverage amounts do not apply where the insurer clearly informs the insured in writing that they do not apply.

8 Statement of David McRae Roberts dated 30 August 2017 (Ex 6.259) at [46]-[48] (ANZ.999.021.0157 at .0167).

Question 6

Is there scope for insurers to make greater use of standardised definitions of key terms in insurance contracts?

23. ANZ supports the use of the minimum standards that are currently set out in the ICA and in LICOP.[9] These minimum standards provide customers with clarity over commonly used terms. Accordingly, ANZ does not oppose greater use of standardised definitions of key terms.

24. Standardised terms offer the greatest utility where they provide a core or minimum standard for commonly used terms, so that customers who take out cover of a particular kind can be satisfied that it will have minimum content. This approach leaves areas for insurance manufacturers to differentiate their product offerings. ANZ submits that it is important that insurers have the ability to meaningfully differentiate their insurance products to maximise competition and consumer choice in the marketplace.

25. However, ANZ does not support additional linking of medical terms in insurance contracts to *changing* definitions for two reasons:

    (a) as it relates to legacy insurance products, the inclusion of altered definitions applied retrospectively would be a substantial change to the originally agreed terms. This would be likely to carry material implications for the sustainability of the product as a whole. This concern is particularly significant in life insurance, where such terms are most common; [10] and

    (b) as it relates to new contracts of insurance, terms that are entered into on the basis that they are subject to change carry an element of uncertainty for both the insurer and insured. That uncertainty makes the risk difficult to accurately price, leading to the risk of under or over insurance.

26. ANZ considers that customers should be free to identify products which provide coverage for the types of medical conditions that concern them. This freedom could be undermined by the imposition of a central definitions structure beyond minimum standards for key terms.

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9 Financial Services Council, *Life Insurance Code of Conduct*, 1 July 2017, Appendix: minimum standard medical definitions.

10 This issue is discussed in response to question 3, above.

C. SALES

Question 7

Should monetary and non-monetary benefits given in relation to general insurance products remain exempt from the ban on conflicted remuneration in Division 4 of Part 7.7A of the Corporations Act 2001 (Cth)? If so, why?

27. Part 7.7A of the Corporations Act prohibits conflicted remuneration. The aim of the regime is to align the interests of those who receive advice with those who give it.[11] The conflicted remuneration provisions are extensive, but include exemptions, including relating to general insurance.[12]

28. General insurance includes, amongst other types of insurance, motor, home, contents and travel insurance policies. ANZ does not manufacture such insurance policies and has not done so since 31 July 2015.[13] Its comments in relation to this issue are therefore necessarily confined to general observations as a distributor of general insurance products. Commissions received by ANZ as a product distributor are not passed on to staff responsible for sales.

29. As a distributor of general insurance product, ANZ incurs costs in marketing, training and compliance in effecting their sale. Those costs are not recovered directly from the consumer. Instead, they form part of the product cost base that is recovered from the insurance manufacturer, largely through commissions. In the event that those commissions were banned, the cost of distributing the insurance would need to be allocated elsewhere.

30. To the extent that the Commission has identified inappropriate sales connected with general insurance, ANZ submits that those issues would be addressed by the reforms referred to in response to questions 4 and the upcoming changes identified in response to question 1, above.

Question 8

Should monetary benefits given in relation to life risk insurance products remain exempt from the ban on conflicted remuneration in Division 4 of Part 7.7A of the Corporations Act 2001 (Cth)? Why shouldn't the cap on such benefits continue to reduce to zero?

31. The conflicted remuneration provisions relating to life insurance advice and information were introduced following extensive review and consideration.

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11 Australian Securities & Investments Commission, *Regulatory Guide 246: Conflicted and other banned remuneration*, [RG246.1], December 2017.

12 *Corporations Act* 2001 (Cth) s 963B(1)(a).

13 ANZ does distribute a direct life product known as ANZ Income Protection which includes two general insurance benefits both of which are issued by OPGI.

32. In 2021, ASIC will conduct a further review to consider whether the new industry arrangements for life insurance advice have better aligned the interests of financial firms and consumers. [14] ANZ considers that the reforms should be permitted to operate as presently formulated for a period of time sufficient to determine their efficacy, before further changes are considered or introduced.

Question 9

Is banning conflicted remuneration sufficient to ensure that sales representatives do not use inappropriate sales tactics when selling financial products? Are other changes, such as further restrictions on remuneration or incentive structures, necessary?

33. The conflicted remuneration regime in the context of insurance sales seeks to align the interests of sales representatives with the interests of consumers. It is part of a range of measures available to encourage sound advice, including: (i) remuneration and incentive structures that reward customer satisfaction and regulatory compliance rather than sales or revenue; and (ii) an increased emphasis on education and training requirements to ensure familiarity with the existing rules and structures in place. A number of initiatives directed to these matters were identified in the course of previous submissions.[15]

34. ANZ submits that the above measures, in combination with the current legislative framework (including the Life Insurance Framework reforms) and ongoing compliance monitoring, substantially reduce the risk of inappropriate sales tactics.

Question 10

Should the direct sale of insurance via outbound telephone calls be banned? If not, is the current regulatory regime governing the direct sale of insurance via outbound telephone calls adequate to avoid consumer detriment? If the current regulatory regime is inadequate, what should be changed?

35. ANZ submits that the direct sale of insurance by *unsolicited* outbound telephone calls to non-customers should be banned. This is consistent with, and builds upon, the current anti-hawking requirements and the obligation to ensure that insurance is suitable for a customer's needs.

36. ANZ submits that the current regulatory regime is otherwise adequate and that the sales of insurance via outbound telephone calls can be appropriate where there is a pre-existing relationship with the customer or where the customer requests contact from the bank to discuss insurance or other products. In such circumstances, telephone sales might be a convenient and appropriate sales method.

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[14] Commonwealth of Australia, *Corporations Amendment (Life Insurance Remuneration Arrangements) Bill 2016: Explanatory Memorandum,* Regulation Impact Statement, [2.34].

[15] See for example *Submissions by ANZ in Respect of General Questions – Round 2 Hearings* dated 7 May 2018 at [37] –[42].

Question 11

Is Recommendation 10.2 from the Productivity Commission's report on "Competition in the Australian Financial System", published in June 2018, sufficient to address the problems that can arise where financial products are sold under a general advice model (for example, the sale of financial products to consumers for whom those products are not appropriate)? If not, what additional changes are required? Are there some financial products that should only be sold with personal advice?

37. ANZ agrees that the term 'advice' in the composite phrase 'general advice' has the capacity to confuse and/or mislead and supports legislative change that would remove the use of that term across the industry. ANZ also agrees that consumer testing is required to identify alternative terminology.

38. It is, of course, open to customers to obtain personal advice concerning their insurance needs. However, ANZ submits that the creation of a personal advice requirement prior to the purchase of insurance products would limit the availability of those products to the community at large and may result in the population being under-insured.

39. ANZ submits that no change is required beyond the DDO currently before the Commonwealth Parliament that oblige manufacturers and distributors not to offer products without identifying the target market and determining that the product would generally meet the likely objectives, financial situations and needs of persons in that target market. If implemented, this will provide a significant safeguard to ensure that insurance products are offered to appropriate customers.

40. These considerations take on additional importance in light of the public benefit from a comprehensively insured population.

Question 12

Should all financial services entities that maintain an approved product list be required to comply with the obligations contained in FSC Standard No 24: Life Insurance Approved Product List Policy

41. ANZ agrees that all financial services entities that maintain an approved product list for life insurance should be required to comply with the obligations contained in FSC Standard No 24: Life Insurance Approved Product List Policy.

D. ADD-ON INSURANCE

Question 13

Should the sale of add-on insurance by motor dealers be prohibited?

42. ANZ does not sell add-on insurance through motor dealers. Consequently, ANZ does not express a view in relation to this question.

Question 14

Alternatively, should add-on insurance only be sold via a deferred sales model? If so, what should be the features of that model?

43. On the assumption that this question is directed to add-on insurance sold by motor dealers, ANZ repeats its response to question 13 above. The application of a deferred sales model to other add-on insurance is addressed in question 15 below.

Question 15

Would a deferred sales model also be appropriate for any other forms of insurance? If so, which forms?

44. ANZ assumes that this question addresses other forms of add-on insurance and responds on that basis.

45. ANZ has supported the application of a deferred sales model to certain forms of add-on insurance under the Australian Banking Association's 2019 Banking Code of Practice. However, ANZ does not support the application of a deferred sales model to mortgage protection insurance (**MPI**).

46. Whilst other forms of add-on insurance products may involve single purpose cover for lower value exposures, MPI relates to transactions of a far more substantial nature. A mortgage often represents the single largest financial commitment a consumer will make. For most home loan borrowers in Australia, the risk against which MPI protects is a material one (ie, the risk that in the event a borrower dies or is otherwise unable to meet loan repayment obligations the mortgaged property may have to be sold).

47. In that context, ANZ considers that a deferred sales model is not appropriate for MPI. Given the high level of mortgage loan debt in Australia, the ability to obtain MPI at the time a customer's risk exposure changes is important and appropriate.

Question 16

If the ban on conflicted remuneration is not extended to apply to general insurance products, should the payment of commissions for the sale of add-on insurance by motor dealers be limited or prohibited?

48. ANZ does not sell add-on insurance through motor dealers. Consequently, ANZ does not express a view in relation to this question.

E. CLAIMS HANDLING

Question 17

Should the obligations in section 912A of the Corporations Act 2001 (Cth) apply to all aspects of the provision of insurance, including the handling and settlement of insurance claims?

Question 18

Should ASIC have jurisdiction in respect of the handling and settlement of insurance claims?

49. ANZ supports:

    (a) the obligations in section 912A of the Corporations Act applying to the provision of insurance in a broad sense including the handling and settlement of claims; and

    (b) ASIC having jurisdiction in respect of the handling and settlement of claims.

50. The mechanism by which such reforms might be given effect would need to be considered to ensure that it did not produce unintended consequences. For example, there could be broader consequences for insurers and their personnel if claim assessors were seen to be providing financial product advice, or dealing in a financial product, in the conduct of claims handling.

Question 19

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?

Question 20

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?

51. Questions 19 and 20 concern similar issues arising from non-disclosure or misrepresentation on the part of an insured (referred to collectively as **non-disclosure** below).

52. The duty of disclosure addresses the information asymmetry that exists between applicant and insurer. An insurer's assessment of the risk arising from an applicant's disclosure informs whether to extend cover (and if so on what terms and at what price).[16] The ability of an insurer to investigate potential non-disclosure at the claims stage and, in extreme cases, to avoid a policy, are important elements of the regime.

[16] See generally, Statement of Gavin Murray Pearce dated 21 August 2018 (Rubric 6-8) at [26]-[27] (ANZ.999.021.0135 at .0146).

53. Imposing claims restrictions as suggested in questions 19 and 20 could mean that a less than truthful applicant is placed in a better position than an applicant who provided truthful and comprehensive information (and was, therefore, denied cover or provided cover on a more expensive or more limited basis). More limited recourse for insurers in cases of relevant non-disclosure could change the risk profile of the insurance pool, which would result in higher costs.

54. ANZ recognises the need to ensure that insurers do not use non-disclosure as a reason to investigate or deny claims inappropriately. However, the current regulatory framework[17] imposes limitations on information gathering and provides for flexible responses that balance the insured's interest in claims not being denied as a result of minor omission or inaccuracy with the insurer's interest (and the interests of insureds more generally) in retrospectively amending or avoiding policies in cases of more material non-disclosure.

Question 21

Should life insurers be prevented from engaging in surveillance of an insured who has a diagnosed mental health condition or who is making a claim based on a mental health condition? If not, are the current regulatory requirements sufficient to ensure that surveillance is only used appropriately and in circumstances where the surveillance will not cause harm to the insured? If the current regulatory requirements are not sufficient, what should be changed?

55. Appropriately conducted surveillance plays a relevant part in the claims handling process. It enables an insurer to assess the veracity of a claim by observing a claimant's functional capacity and by determining whether their actual activities are consistent with reported limitations.

56. ANZ recognises that claimants with mental health conditions may be particularly vulnerable to adverse impacts arising from surveillance. For this reason, OPL's surveillance activities in relation to mental health claims are subject to further safeguards, which require a *prospective* consideration of the appropriateness of surveillance having regard to the detriment it might pose to a particular claimant. In this way, OPL's processes go beyond clause 8.12(f) of LICOP, which requires only that surveillance be *discontinued* where there is evidence from an independent medical examiner that it *is* negatively impacting a claimant's recovery.

57. Under OPL's Surveillance in Claims Management Protocol, surveillance should never be considered where the claimant or their doctor report that: [18]

(a) the claimant is or has recently been suicidal;

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[17] See for example Financial Services Council, *Life Insurance Code of Practice*, 1 July 2017, cl 8.5 (information gathering) and ICA s 29 (remedies).

[18] Statement of Gerard Francis Kerr dated 23 August 2018 dated 23 August 2018 (Rubric 6-18) at [162]-[163] (ANZ.999.021.0001 at .0035-.0036) and Exhibit GFK-41 to the Gerard Francis Kerr statement p 3 (ANZ.801.009.1081 at .1083).

(b) the claimant is diagnosed with schizophrenia or another condition causing severe paranoia or hypervigilance and is currently experiencing symptoms (or has had a recent episode); or

(c) observations could be detrimental to the claimant's health.

58. ANZ would support the adoption of the above prospective safeguards in LICOP to ensure that surveillance is only used appropriately and with a view to minimising the risk that it will cause harm to the insured.

Question 22

Should the General Insurance Code of Practice be amended to provide that, when making a decision to cash settle a claim, insurers must:

22.1 act fairly; and

22.2 ensure that the policyholder is indemnified against the loss insured (as, for example, by being able to complete all necessary repairs)?

59. ANZ does not provide claims handling services in respect of the general insurance products it offers in the categories of motor, home, contents and travel insurance. Consequently, it does not express a view in response to this question.

F. INSURANCE IN SUPERANNUATION

Question 23

Should universal:

23.1 minimum coverage requirements; and/or

23.2 key definitions; and/or

23.3 key exclusions,

be prescribed for group life policies offered to MySuper members?

60. The provision of universal minimum coverage and the use of universal definitions and exclusions in 'default' group life insurance products for MySuper members gives rise to a number of complex issues, depending on the scope of such coverage, definitions, and exclusions. In the absence of a detailed proposal for consideration, ANZ does not presently express a view in response to this question.

Question 24

Should group life insurance policies offered to MySuper members be permitted to use a definition of "total and permanent incapacity" that derogates from the definition of "permanent incapacity"

contained in regulation 1.03C of the Superannuation Industry (Supervision) Regulations 1994 (Cth)?

61. Subject to the current prohibition on insurance policies using claim terms that are wider than the *Superannuation Industry (Supervision) Act 1993* (Cth) (**SIS Act**) and the Superannuation Industry (Supervision) Regulations 1994 (Cth) (**SIS Regulations**) conditions of release, group life insurance policies offered to MySuper members should be permitted to use a definition of 'total and permanent incapacity' that differs from the definition of 'permanent incapacity' in the SIS Regulations. If insurers were required to use the definition of 'permanent incapacity' in the SIS Regulations as the definition for 'total and permanent incapacity' (or the equivalent concept) in their policies, this could have unintended consequences for pricing and availability of coverage for members.

Question 25

Should RSE Licensees be obliged to ensure that their members are defaulted to statistically appropriate rates for insurance required to be offered through the fund under section 68AA(1) of the Superannuation Industry (Supervision) Act 1993 (Cth)?

62. At present, section 68AA of the SIS Act does not expressly require RSE Licensees to ensure that members are defaulted to statistically appropriate rates for insurance. Trustees are, however, subject to general duties, such as the requirement to act in members' best interests and the requirement to formulate, review regularly and give effect to an insurance strategy for the benefit of members.[19]

63. For the purpose of responding to this question, ANZ understands that 'statistically appropriate rates for insurance' are those that reasonably reflect the demographics or other attributes (such as occupation, industry and salary) of the members insured under a particular policy.

64. A trustee is required to have regard to the demographic composition of members of the fund in formulating and reviewing its insurance strategy. That information (and any available information about the other attributes of members) will be relevant to the trustee's decisions about the insurance arrangements to be offered to MySuper members under section 68AA(1) of the SIS Act.

65. Where such member information is available, it will be appropriate for a trustee to use that information in designing an insurance offering for its cohort of members.

66. However, in some cases, the information that a trustee has about its members may be limited, unavailable, or available but not independently verified (for example, information about members that is provided to the trustee by members' employers). This may particularly be the case for trustees with funds that contain a broad spectrum of members

[19] SIS Act s 52.

employed in different industries. In such circumstances there may be considerable variation in the individual attributes of members and, therefore, in the ability of a trustee to negotiate statistically appropriate rates for any one particular member (or sub-set of members) or to ensure that the member (or sub-set of members) is defaulted to a rate that is in fact statistically appropriate for them. Any obligation to ensure that members are defaulted to statistically appropriate rates for insurance must therefore be sufficiently flexible to account for such matters. ANZ considers that the general obligations imposed on trustees presently serve that purpose.

Question 26

Should RSE Licensees be prohibited from engaging an associated entity as the fund's group life insurer?

67. For the purpose of responding to this question, ANZ has applied the definition of 'associated entities' contained in section 50AAA of the Corporations Act.

68. ANZ does not consider that RSE Licensees ought to be prohibited from engaging an associated entity as a group life insurer for a fund. RSE Licensees are subject to requirements to act in the best interests of members and avoid or manage conflicts. These obligations extend to the procurement of insurance on behalf of members. It is not, therefore, necessary to specifically prohibit arrangements with associated entities.

69. Insurance acquired from an associated entity is not inherently uncompetitive or undesirable. An associated entity may offer insurance cover at a price more competitive than other providers, or on particular terms that may, in all of the circumstances, be in the best interests of members.

Question 27

Alternatively, should RSE Licensees who engage an associated entity as the fund's group life insurer be subject to additional requirements to demonstrate that the engagement of the group life insurer is in the best interests of beneficiaries and otherwise satisfies legal and regulatory requirements, including the requirements set out in paragraphs 22 to 24 of Prudential Standard SPS 250, Insurance in Superannuation?

70. ANZ does not oppose the introduction of a requirement that trustees demonstrate their compliance with their legal and regulatory requirements in respect of engagement of group life insurers. For this purpose, ANZ understands a requirement to 'demonstrate' such matters would involve a reporting obligation that would apply in addition to the current requirements for trustees to *be able to demonstrate* to APRA that the engagement of a group life insurer is conducted at arm's length and is in the best interests of members.

71. Any such proposal ought to specifically identify the matters to be addressed in reports made under proposed reporting obligations, to ensure clarity for trustees in complying with those obligations.

Question 28

Are the terms set out in the Insurance in Superannuation Voluntary Code of Practice sufficient to protect the interests of fund members? If not, what additional protections are necessary?

72. The Insurance in Superannuation Voluntary Code of Practice (**Code**) was published in December 2017. The Code represents the outcome of work by the Insurance in Superannuation Working Group (comprising representatives from superannuation funds and bodies, the Australian Institute of Superannuation Trustees (**AIST**), the Association of Superannuation Funds of Australia (**ASFA**), the FSC, life insurers, and consumer advocates) over the course of approximately one year.

73. Broadly, the Code sets standards in respect of insurance in the superannuation industry that aim to provide greater understanding, clearer accountability, and consistency of delivery across the industry. Its provisions address matters such as the provision of appropriate and affordable cover and helping members to make informed decisions. Clause 2.1 of the Code states that its overarching objective is to improve the insurance in superannuation offered to members and the processes by which insurance benefits are provided to them.

74. The Code commenced on 1 July 2018, and entities that adopt the Code are required to publish an implementation plan by 31 December 2018. The Code does not, however, require funds to be fully compliant until 30 June 2021. During this time, representatives of AIST, ASFA and the FSC will continue to meet and consider issues in respect of the Code as and when they arise. In particular, clause 14.7 provides that the Insurance in Super Code Owners will commission formal independent reviews of the Code as necessary, no later than every 3 years. Reviews will focus on whether the Code is meeting its objectives, in particular, whether the Code has improved the insurance offered in superannuation and the processes by which insurance is delivered. At present, ANZ considers that the provisions of the Code are sufficient to protect the interests of the fund members, but acknowledges that this should be revisited with each formal independent review of the Code.

75. In a more general sense, however, ANZ supports the proposal for the Code to be made mandatory (rather than voluntary).

G. SCOPE OF THE *INSURANCE CONTRACTS ACT 1984* (CTH)

Question 29

Is there any reason why unfair contract terms protections should not be applied to insurance contracts in the manner proposed in "Extending Unfair Contract Terms Protections to Insurance Contracts", published by the Australian Government in June 2018?

76. The existing UCT laws should be incorporated into the ICA with recognition of the unique aspects of life insurance arrangements to ensure there are no adverse unintended consequences.

77. Specifically, reforms should have regard to the long term and guaranteed renewable nature of life insurance products, the requirement for insurers to prudentially manage risks, and the reinsurance arrangements that apply to contracts of that kind. Further, life insurers should be given a reasonable period to amend their contracts before the new regime commences.

78. ANZ submits that any such new regime should only be applied prospectively and should have the following elements insofar as it applies to life insurance contracts:

(a) the 'main subject matter' of an insurance contract should be defined broadly to include terms that define the scope of cover;

(b) clarification should be provided that the 'upfront price' will include the premium and the waiting period, as well as additional premiums, fees or charges that are payable by the policyholder, regardless of the stage in the policy's life, and that these will not be subject to review;

(c) for long term life policies, it should be made clear that a term which provides a life company with the ability to unilaterally increase or decrease premiums will not be considered unfair where the increase is related to the management of the insurer's risk and is consistent with the other requirements of the *Life Insurance Act 1995* (Cth);

(d) examples specific to insurance ought to be added to the list of examples of the kinds of terms that may be unfair. However, this should be provided through regulation and following consultation;

(e) where a term is found to be unfair, as an alternative to the term being declared void, a court should be able to make other orders if it deems that more appropriate; and

(f) ASIC should be given the power to exempt or declare that a term of a life insurance product is not subject to the UCT regime (either at all, or in particular circumstances).

79. Amendments of this kind are likely to require substantial additional and specific consultation, and be subject to review following initial implementation to ensure that they are having the desired effect.

Question 30

Does the duty of utmost good faith in section 13 of the Insurance Contracts Act 1984 (Cth) apply to the way that an insurer interacts with an external dispute resolution body in relation to a dispute arising under a contract of insurance? Should it?

80. The duty of utmost good faith in section 13 of the ICA applies to both the insurer and the insured in their dealings with one another under or in relation to their contract of insurance. The High Court in *CGU v AMP*[20] observed that the duty of good faith requires an insurer to do more than act honestly and may require it to have regard not only to its own interests, but also to the legitimate interests of its insured.

81. An external dispute resolution body exists to facilitate a resolution of a dispute between the insurer and insured, through either mediation or an adjudication process.

82. Where an insurer deals with an insured either directly, or through the framework of an external dispute resolution body, then the duty of utmost good faith will necessarily inform the way in which it does so. The dispute resolution bodies have terms of reference to which insurers are party. If the insurer breaches those terms, then that breach should be dealt with as a matter of enforcing the framework governing the relationship between the insurer and the dispute resolution body.

83. ANZ submits that it is not necessary or appropriate to impose a duty of good faith on an insurer in its interactions with a dispute resolution body in addition to the insurer's existing obligations referred to above. The legitimate interests of the dispute resolution body are to have both parties conduct the dispute in accordance with its terms of reference, so as to facilitate an impartial resolution of the dispute by the dispute resolution body.

Question 31

Have the 2013 amendments to section 29 of the Insurance Contracts Act 1984 (Cth) resulted in an "avoidance" regime that is unfairly weighted in favour of insurers? If so, what reform is needed?

84. The 2013 amendments to section 29 of the ICA were the culmination of nearly a decade-long consultation period between stakeholders following the release of the 2004 Milne Cameron report into possible reforms of the ICA.[21] ANZ understands that the

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[20] (2007) 235 CLR 1.

[21] The Treasury, *Review of the Insurance Contracts Act 1984 (Cth): Final Report on Second Stage: Provisions other than section 54,* Report(2004).

amendments to section 29 were primarily directed at providing more flexible, proportionate remedies for pre-contractual non-disclosure and misrepresentation rather than policy avoidance *per se*. Such an approach was more suited to modern life insurance products.

85. ANZ does not accept that the amendments have created an 'avoidance regime'. However, it is possible that they have operated in an unintended way, including by operating against the interests of consumers in some instances.

86. ANZ considers that reform in this area is needed to remedy the anomalies that arose following the 2013 amendments. However reforms should be consistent with the overarching views of the Milne Cameron report (which received support from all stakeholders). Specifically, life insurers should retain the right to:

(a) avoid cover at any time on the basis of pre-contractual fraudulent and material misrepresentation or non-disclosure;

(b) avoid cover within 3 years on the basis of 'innocent' pre-contractual material misrepresentation or non-disclosure when the misrepresentation or non-disclosure is so profound that the life insurer would not have issued any cover under the policy had it known the true facts; and

(c) utilise the proportionate response and vary cover as envisaged by the current sections 29(4) and 29(6) of the ICA when it does not choose to avoid cover.

Question 32

Does the duty of disclosure in section 21 of the Insurance Contracts Act 1984 (Cth) continue to serve an important purpose? If so, what is that purpose? Would the purpose be better served by a duty to take reasonable care not to make a misrepresentation to an insurer, as has been introduced in the United Kingdom by section 2 of the Consumer Insurance (Disclosure and Representations) Act 2012 (UK)?

87. Section 21 of the ICA continues to serve an important purpose. This section ensures the disclosure necessary to properly understand and price the risk involved in the contract of insurance. In combination with section 29 of the ICA (discussed in response to question 33 below), it is a key protection for an insurer that may be entering into a long term insurance contract.

88. This purpose would not be better served by a duty to take reasonable care not to make a misrepresentation to an insurer. The duty of disclosure is an important part of the insurance relationship and ANZ considers that it is in the interests of both the insured and the insurer for the disclosure to be retained and simplified. The duty of fair representation under the *Consumer Insurance (Disclosure and Representations) Act 2012* (UK) does not ensure that the necessary disclosures are made by the insured, as it simply requires that

the insured take reasonable care not to make a misrepresentation when answering an insurer's questions.

H. REGULATION

Question 33

Should the Life Insurance Code of Practice and the General Insurance Code of Practice apply to all insurers in respect of the relevant categories of business?

89. ANZ supports the extension of LICOP and the General Insurance Code of Practice (together the **Codes**) to all insurers and reinsurers in respect of the relevant categories of business.

Question 34

Should a failure to comply with the General Insurance Code of Practice or the Life Insurance Code of Practice constitute:

34.1 a failure to comply with financial services laws (for the purpose of section 912A of the Corporations Act 2001 (Cth));

34.2 a failure to comply with an Act (for example, the Corporations Act 2001 (Cth) or the Insurance Contracts Act 1984 (Cth))?

90. ANZ takes its obligations under the Codes seriously and reports to the Life Insurance Code Compliance Committee and the General Insurance Code Governance Committee on compliance measures under each Code.

91. However, the Codes were not drafted with a view to incorporation into either the Corporations Act or the ICA. They were instead drafted by reference to detailed operational matters, procedural steps and best practice guidelines that are not easily translated to a statutory setting[22] and breach of which should not be deemed unlawful or attract penalty under either the Corporations Act or the ICA.

92. Further, ANZ submits that key obligations, such as the duty of utmost good faith, disclosure, and various time limits in relation to responding to complaints, are already enshrined in statute and regulations.

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[22] For example, clause 5 of the Life Code provides a requirement to make a decision within five business days (clause 5.4) but is subject to other information gathering powers (clause 5.5 and 5.6); Clause 9.10 of the Life Code requires a response to a complaint within 90 days "*where possible*".

Question 35

What is the purpose of infringement notices? Would that purpose be better achieved by increasing the applicable number of penalty units in section 12GXC of the Australian Securities and Investments Commission Act 2001 (Cth)? Should there be infringement notices of tiered severity?

93. Infringement notices provide a response to wrongdoing that is capable of being deployed quickly and with clear effect. Because they do not result in formal findings, they can be used cost effectively without the need to conclude complex disputes. They are appropriate for less serious contraventions, where public denunciation might be balanced against the cost and delay involved in seeking formal findings.

94. The amount of an infringement notice operates as a deterrent, particularly since it is typically open to regulators to issue multiple infringement notices to reflect their view of the gravity of the conduct. So do the reputational consequences arising from having such a notice issued against an entity.

95. ANZ notes recommendation 45 of the ASIC Enforcement Review that penalties for new infringement notices should be set at 12 penalty units for individuals and 60 penalty units for corporations and that current penalties should be left unchanged, for the reasons given in the Final Report.[23] If, contrary to this submission, the Commission contemplated a further increase to the number of penalty units available for sanctioning such conduct, it would not serve community expectations unless it was associated with additional discretion to ensure that the amount is proportionate to the wrongdoing in question, so that the mitigating or aggravating factors could be taken into account.

I. COMPLIANCE AND BREACH REPORTING

Question 36

Is there sufficient external oversight of the adequacy of the compliance systems of financial services entities? Should ASIC and APRA do more to ensure that financial services entities have adequate compliance systems? What should they do?

96. ANZ considers that each of APRA and ASIC have effective tools at their disposal to adequately oversee the compliance systems of financial services entities. ASIC oversees compliance through surveillance, and where appropriate, formal investigations which may lead to enforcement actions. ANZ supports the expansion of ASIC's activities to include embedding staff within the bank as a means of monitoring compliance.

97. APRA undertakes external oversight principally through its supervisory activities. CPS 220 requires APRA-regulated institutions to annually assess their risk management framework which is subject to a comprehensive review by operationally independent persons at least

[23] The Treasury, *ASIC Enforcement Review: Taskforce Report,* December 2017, 83-84.

every three years. This provides a useful starting point for APRA's understanding of entities' systems. In addition, ANZ regularly meets with APRA to discuss ANZ's operational risk and compliance framework and systems. ANZ has found that this has been usefully supplemented by a formal quarterly update with APRA. Further, APRA is empowered to, and does, request information in relation to specific issues around governance and compliance frameworks (including in relation to compliance systems) and call on financial institutions to provide an assessment of their risk and governance frameworks – as it has done following publication of the CBA Prudential Inquiry Final Report. APRA has the ability to take enforcement action in appropriate cases.

98. Each of ASIC and APRA have deployed the tools at their disposal in various ways. For example, in 2015, ASIC carried out a significant in-depth review of OPL's compliance processes and procedures. OPL found that process to be of value in evaluating its compliance framework. By way of further example, in 2017, APRA undertook an in-depth review of the IT risk framework of the major banks, following which ANZ made a number of improvements to its operational risk and compliance framework for technology risks, created additional positions for technology risk specialists and provided, and continues to provide, quarterly updates to APRA on ANZ's progress in the implementation of further improvements.

99. ANZ acknowledges the Commission's view that a greater emphasis on compliance is required and supports measures taken by ASIC to broaden its lines of inquiry and ask more questions about entities' overall control environment in the course of their surveillance activities.

Question 37

Should there be greater consequences for financial services entities that fail to design, maintain and resource their compliance systems in a way that ensures they are effective in:

37.1 preventing breaches of financial services laws and other regulatory obligations; and

37.2 ensuring that any breaches that do occur are remedied in a timely fashion?

100. ANZ notes that the Treasurer has announced the intended introduction of a bill into Parliament that, if enacted, would increase the consequences for contraventions of the financial services law.[24] ANZ considers that the Banking Executive Accountability Regime (**BEAR**) is also an important feature of the current regulatory landscape, which will increase accountability of both financial services entities and individuals for the design, maintenance, and resourcing of prevention and remediation systems.

[24] Media release issued by the Treasurer *Strengthening Penalties for white collar crime* (21 October 2018).

101. In considering what consequences should be imposed in particular cases, ANZ acknowledges that an effective regulator must demonstrate a preparedness to pursue enforcement action if compliance is not forthcoming.

102. In undertaking compliance action, it is appropriate to respond proportionately to the conduct in question. It follows that increased penalties for deliberate misconduct are appropriate.

103. Compliance failures can arise even where care and diligence has been demonstrated in system design, operation and/or remediation. ANZ submits that there should be capacity to take into account genuine efforts in determining consequences for breaches of financial services obligations or the time involved in effecting customer remediation. This is consistent with general approaches to breaches of legislation and encourages meaningful engagement with regulators.

Question 38

When a financial services entity identifies that it has a culture that does not adequately value compliance, what should it do? What role, if any, can financial services laws and regulators play in shaping the culture of financial services entities? What role should they play?

104. It should be expected that financial services entities will articulate and profess standards of conduct and behaviour that are consistent with the expectations expressed by the community and set out in law. An effective way to improve culture is to influence the 'tone from the top', including the extent to which junior staff are encouraged to identify and escalate any inappropriate conduct.

105. It is impossible to eliminate all compliance failures. Where material failures occur within organisations, the appropriate measure of conduct and culture will be the ability to address compliance failures and, where appropriate, notify regulators with details of the breach (as well as any remediative action taken). The speed with which these steps are carried out may also be a measure of conduct and compliance culture.

106. The steps that will be appropriate to respond to identified cultural deficiencies will depend upon the nature of the deficiencies identified and may include:

(a) clearly identifying values that are consistent with the target culture;

(b) ensuring such values are modelled from the 'top' down;

(c) reviewing processes in the workplace to ensure that they reflect the target culture (including external review);

(d) considering whether remuneration structures properly reflect the target culture and making changes to ensure that they do so in the future;

(e) reinforcing and rewarding conduct that is in line with good conduct and values in the organisation, including by calling out inappropriate conduct; and

(f) ensuring staff are accountable for decisions and actions, both under BEAR and at more junior levels, by taking appropriate disciplinary action in response to unacceptable conduct.

107. ANZ has taken or is taking steps including the above in its ongoing efforts to promote a culture in line with its values and purpose. Where cultural deficiencies are identified, it presents an opportunity to consider root causes and realign or refocus those efforts to address those deficiencies. The culture of any organisation requires ongoing attention and calibration.

108. Regulators can have a constructive role in effecting cultural change of this kind, including by providing examples of best practice (or poor practice), or guidelines about embedding positive values and performance measures. ASIC's program to embed staff within the banks may also have a positive influence on culture over time.

Question 39

Are there any recommendations in the "ASIC Enforcement Review Taskforce Report", published by the Australian Government in December 2017, that should be supplemented or modified?

109. ANZ does not consider that the recommendations of the ASIC Enforcement Review Taskforce Report should be supplemented or modified at this stage. ANZ submits that, subject to how they are implemented, these recommendations, along with the DDO and PIP (if passed) and the embedding of ASIC officers in the 'big four' banks and AMP, should provide ASIC with sufficient and appropriate regulatory tools to perform its functions.

25 October 2018