CALI Council of Australian Life Insurers

Lead Ombudsman - Superannuation
Australian Financial Complaints Authority
GPO Box 3
Melbourne VIC 3001

By email: consultation@afca.org.au
cc: Emma Curtis

11 October 2024

Dear Ms. Gray (Heather),

Response to the joint consultation on superannuation Approaches

We appreciate the opportunity to respond to the Australian Financial Complaints Authority's (AFCA) consultation on superannuation Approaches. Our aim is to foster a collaborative and constructive relationship with AFCA. We want to provide clear feedback that supports a fair approach while acknowledging the operational realities that insurers face, ensuring everyone is on the same page when it comes to making decisions that impact the industry and our customers.

We are grateful for the roundtable held on 3 October to discuss many of the issues we raise below. We found it a very useful and collaborative discussion and appreciate the open and transparent approach AFCA took at the meeting. We recommend similar formats of engagement so that we can more efficiently raise and clarify issues with the AFCA team.

The below provides a record of some of the concerns raised at the meeting and goes into further detail to help guide drafting amendments that may be made by AFCA. We have also attached a marked-up draft of the Approach to sections 29(6) and 29(7) of the Insurance Contracts Act 1984 (Cth) for consideration.

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Key points in this submission

- We believe it is important the documents reflect the interpretation of the law, especially about types of evidence and the applicability of statements; good faith and fairness; reviewing an insurers decision; and, ensuring consistency with the rest of section 29 of the ICA when it comes to accessing a s29 remedy per "relevant failure".
- We are concerned that the draft Approach document implies a requirement to compare an insurer's exclusion wording with that of other insurers under section 29(6), which exceeds the authority granted by the Insurance Contracts Act 1984 (ICA) because section 29(6) does not mandate such a comparison.
- It is important not to create additional obligations in the documents beyond what is articulated in the Life Insurance Code of Practice (the Life Code) and law.
- We believe the documents should refer to and/or directly reference the Life Code as the Code reflects good industry practices (e.g. on fairness and reasonableness).
- We believe the case studies unintentionally misrepresent current industry practices and how the law is typically interpreted. We've suggested alternatives that more accurately align with the intended purpose of the draft.

This letter is intended to highlight some of the areas in the current drafts that are of a concern. For instance, in the Approach to sections 29(6) and 29(7) of the Insurance Contracts Act 1984 (Cth), AFCA's proposal to compare the wording of the exclusion applied by the insurer with those applied by other insurers, and to vary the exclusion so that the wording is 'not inconsistent', is not open to it under the restrictive wording of section 29(6).

Similarly, AFCA's proposal to require statement(s) from reinsurers or external consultants under section 29(7) raises some practical concerns. While we understand the intent, we do not believe it is necessary to provide a statement from a reinsurer or external consultant in order for a fair decision to be reached, especially as reinsurers are not party to the complaint. If it were applied, it would lead to process delays, unnecessary complexity in managing complaints and inconsistent results. In keeping with the intent of the AFCA Rules and Operational Guidelines where complaints will be considered in a way that is efficient, effective and timely, expecting insurers to engage with third party reinsurers for statements in the context of disputes, particularly where reinsurers are not parties and have no obligations to comply, will work against that intent.

A more practical solution would be accepting reinsurer guidelines as evidence to support an insurers s29(7) positions to demonstrate that their variation (e.g. the application of an exclusion) is not inconsistent with market practice, which would ensure consistency and efficiency, as well as be a cost-effective approach. This would promote both fairness and operational feasibility, fostering greater confidence in the process. We understand AFCA has accepted this in previous determinations, for example Determination 818374, and so would be consistent with positions taken by AFCA. We further note that AFCA's Operational Guidelines confirm that it is not a Court, and does not require parties to give evidence under oath or cross-examination. Therefore, we feel the requirement for statements from third parties is not consistent with this position. We have suggested an amendment to the draft Approach Paper to include reference to evidence of this nature and removed reference to statements being required from third parties and/or reinsurers.

Similarly, we think it's essential for AFCA to clarify what it means when it says it will assess whether an insurer's decision was "unfair" or "unreasonable." If an insurer has met all its obligations under sections 29(4) and 29(6), it's hard to see how applying the appropriate remedy could be considered unfair. Clear guidance from AFCA here would help insurers understand how these terms will be applied.

Overall, we want to make sure that any documents that are for public consumption are balanced and practical, and that insurers can engage meaningfully with AFCA. This will help us avoid unnecessary complications and keep the focus on fair outcomes for all involved.

We have set out our concerns as follows, adopting the headings in the draft Approach Paper.

Approach to sections 29(6) and 29(7) of the Insurance Contracts Act 1984)

1.2 Summary (page 2)

We propose adjusting the first bullet point to include:

- *a misrepresentation made by the insured or life insured where they have breached their duty to take reasonable care not to make a misrepresentation (for consumer insurance contracts)*

This ensures the wording aligns with section 27AA(2) of the Insurance Contracts Act (ICA), which clearly includes the life insured. Including this small but important clarification helps ensure that our understanding aligns with legal obligations.

Reviewing the insurer's decision (page 3)

Section 1055 of the Corporations Act obliges AFCA to affirm a decision if it is fair and reasonable in all the circumstances. Our concern lies with AFCA's suggestion that it may consider whether an insurer acted "unfairly or unreasonably." While fairness is the foundation of all decision-making, we believe it is important to consider this within the existing legal framework that governs insurers' rights to exercise remedies under sections 29(4) and 29(6). If an insurer has legally satisfied all requirements, it's challenging to identify scenarios where such an action could be deemed unfair. Clearer guidelines from AFCA on this point would help ensure decisions are well understood and perceived as just.

Good Faith, Fairness, and Legal Consistency

We believe AFCA's approach to good faith and fairness should focus on how insurers investigate and communicate decisions regarding non-disclosure. This is already addressed in the Life Insurance Code of Practice, which sets out the responsibilities of insurers to act in good faith and communicate clearly with insured parties (e.g. Clause 5.14 on investigating a relevant failure, and Clause 3.16 on show cause procedures).

We believe it is essential that the Approach Paper doesn't inadvertently create new obligations beyond what is already articulated in the Code and law. The section 29(6) remedy should be assessed based on whether it is consistent with the law, and section 29(7) already provides adequate safeguards for fairness and consistency.

We also feel the document would benefit from offering clarification on AFCA's approach when a section 29(6) variation is legally valid but there are process issues, such as missing a show cause notice, to ensure there is clarity for customers who may read the document.

Not inconsistent with other reasonable and prudent insurers (page 6)

We acknowledge AFCA's goal of ensuring fair underwriting decisions, but requiring specific exclusion wordings from other insurers presents practical challenges. Insurers often cannot access proprietary exclusion wording from competitors, especially when decisions are made years after the fact. Additionally, underwriters cannot provide this level of detailed information from past employers.

AFCA's Approach Paper, on pages 6 and 7, and Case Study 2 appears to suggest that AFCA considers that the section 29(7) test requires a comparison of different insurers' exclusion wording when applying a section 29(6) variation to impose an exclusion. For instance, on page 7, AFCA suggests that when a variation to impose an exclusion is made, evidence of the "specific wording" that would have been applied by other reasonable and prudent insurers is necessary.

We believe this is necessary to clarify because section 29(6) allows insurers to place themselves in the position they would have been in if the relevant failure by the life insured hadn't occurred. This means the insurer can apply its own exclusion wording, but section 29(6) does not require an insurer to adopt the exclusion wording from another insurer's policy or underwriting guidelines.

Section 29(7) requires the insurer to show that its decision is not inconsistent with what other reasonable and prudent insurers would have done under similar circumstances at the time. This doesn't mean identical wordings must be used, but rather that other reasonable insurers would have taken a comparable approach to the situation. Insurers have different risk appetites and underwriting practices, and it's crucial that this is reflected in the document to avoid impacting innovation or competition by requiring insurers to align on specific wording.

The objective of section 29(7) is to ensure that the insurer's variation under section 29(6) isn't an outlier and is supported by practices in the market at that time. However, comparing specific exclusion wordings between insurers isn't necessary to meet this requirement. It's enough to show that other insurers would have applied a similar exclusion to demonstrate compliance with section 29(7).

We feel the Approach Paper currently interprets section29(7) too narrowly and fails to have regard to the operative provisions of section 29(6), by focusing on the exact wording of exclusions, which could have unintended consequences for competition and intellectual property rights in the industry. Insurers should be able to demonstrate compliance by showing that other reasonable insurers would not have offered cover on standard terms without having to disclose proprietary exclusion wording from competitors. Additionally, the variation

should be considered at the time the cover commences, not at the point of claim, as this is irrelevant under section 29(6).

As AFCA has rightly acknowledged, section 29(7) does not require all insurers to reach the same conclusion. Some variation is acceptable as long as the decision is “not inconsistent” with the position of other reasonable and prudent insurers. Therefore, the focus should remain on the decision itself and not on specific exclusion wording. We also believe that AFCA should not rely on Case Study 2 as support for the current approach, as this study was presented to highlight issues with the interpretation of section 29(7), not to justify it.

The language, scope, and effect of the insurer’s variation of the contract (page 5)

When AFCA considers varying or setting aside an insurer’s decision to apply an exclusion, it’s critical that insurers are given procedural fairness, allowing them to respond to any substantial changes in the contract terms. This will help avoid any unintended consequences and provide insurers with the opportunity to address AFCA’s concerns constructively before a final determination is made.

We propose amending wording to recognise that in group superannuation contracts, communication is often managed through trustees, which may not always permit direct contact with life insured members.

Case Study 2 (page 9)

The wording in Case Study 2 refers to the complainant “living with depression,” which could unintentionally mislead about the basis for claims. In our experience, income protection (IP) and total and permanent disability (TPD) claims are based on a person’s inability to work due to disability, not simply “living with” a condition. Adjusting the wording to reflect that claims were made based on “disability arising from” a specific condition will help clarify the case’s relevance and avoid misunderstandings.

As mentioned above, we also believe that Case Study 2 should be an entirely different case, as the detail in this case was conducted to shed light on the challenges surrounding the interpretation of section 29(7) rather than to endorse it.

We have provided an alternative case study below, largely based on AFCA Determination 818374, which we feel would be more suitable to exemplify the point the document is trying to make.

Case study 2 – section 29(7) of the ICA satisfied

A complainant lodged a complaint with AFCA after an insurer varied their Income Protection (IP) cover under section 29(6) of the Insurance Contracts Act (ICA). The complainant had made an IP claim due to chronic nerve pain.

During the claim assessment, the insurer determined that the complainant had made relevant failures in relation to their history of back problems and shoulder pain when they applied for cover and decided to vary the contract under section 29(6) of the ICA by applying a retrospective back exclusion and a retrospective shoulder exclusion. The insurer said this retrospective exclusion effectively defeated the IP claim and denied the claim on this basis. These were the decisions under review in the complaint.

The AFCA decision maker was satisfied that the complainant had made relevant failures by failing to tell the insurer about their history of back and shoulder problems in the application for cover. AFCA was also satisfied with the evidence of the insurer that it would only have issued the cover with a back exclusion and a shoulder exclusion.

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The insurer provided a statutory declaration from one of its underwriters, who had access to reinsurance guidelines used by other insurers, and who confirmed that the guidelines showed that other reasonable and prudent insurers would also have applied a back exclusion and a shoulder exclusion to the IP cover. As such, the AFCA decision maker was satisfied that the insurer had met the requirements under section 29(7) of the ICA, to support the retrospective application of the exclusions.

AFCA was therefore satisfied that the insurer had appropriately varied the IP cover under s29(6) by applying the back exclusion and the shoulder exclusion.

However, AFCA was not satisfied that the evidence showed that the claimed condition was excluded by either the back exclusion or the shoulder exclusion. As such, the AFCA decision maker determined that the insurer must commence paying the IP benefits.

Consistent with the rest of section 29 of the ICA

As mentioned, we believe it is important the Approach documents are consistent with the law. One area where we are concerned the drafting strays from this is the access to applying remedies for insurers.

It's important to maintain flexibility when insurers are dealing with multiple misrepresentations by a policyholder. In instances where there are separate misrepresentations, the insurer should retain discretion in applying appropriate remedies for each misrepresentation, as supported by the wording in section 29, which uses singular language: "a relevant failure." A life insurer should be able to access a s29 remedy per "relevant failure" (i.e. misrepresentations).

The current draft Approach implies an insurer will be limited to just applying either s29(6) or s29(4) remedy per contract, even if there were multiple misrepresentations.

For example, if a life insured made 2 separate misrepresentations, and the insurer would have applied an exclusion as a result of the first misrepresentation, and then a loading as a result of the second misrepresentation – in those circumstances, the insurer should have the discretion to apply the following remedies:

- In relation to the first misrepresentation: apply an exclusion under s29(6)
- In relation to the second misrepresentation: apply either a loading under s29(6) **OR** reduce the sum insured under s29(4).

However, the draft Approach is written in a way that suggests an insurer will not be able to apply s29(4), because s29(6) has already been applied due to the first misrepresentation. Case study 1 provided in the Approach document is concerning as it appears to restrict the remedies available to an insurer.

Thus, there is concern that the approach outlined in the document appears to limit insurers' options, forcing them to choose between remedies under section 29(6) or 29(4) when both might be appropriate for different failures. Ensuring that insurers have access to the full suite of remedies is consistent with the law, important for fair outcomes and is consistent with a number of Determinations made by AFCA in relation to this issue. We would value drafting changes to this effect.

Unbundling & Death Cover

We suggest that the Approach Paper could include a note that the relevant contract of insurance must be unbundled under section 27A of the ICA before a section 29(6) remedy can be applied. Unbundling is a necessary legal step in this process.

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Unintended Consequences of Drafting

Finally, there are a few drafting choices in the current Approach paper that could, in our view, lead to unintended consequences for both insurers and customers. We've suggested amendments to resolve these issues in the attached marked-up document. These amendments aim to prevent complications that could arise from misinterpretation of the ICA.

Approach to delayed insurance claims in superannuation

Unreasonable Delay – Page 2

We think it would be helpful if the Approach Paper clarified what constitutes an 'unreasonable delay.' Delays can occur due to factors beyond the control of the insurer or trustee during the assessment process, and these shouldn't be considered unreasonable. Section 6.18 and 6.24 of the Life Code outline the insurer's obligations to manage delays fairly and to communicate effectively with claimants when delays occur, including how insurers are not held accountable for delays caused by factors beyond their control. These can include awaiting critical information from third parties (e.g., medical reports, financial information) or waiting for the claimant to attend required assessments. The Code specifies that in such cases, insurers must keep claimants informed and explain the reasons for the delay.

Importantly, the Code emphasises that if delays are caused by external factors or are beyond the control of the insurer or trustee, these delays are not to be considered unreasonable, provided that clear communication and updates are given. We therefore feel it is important the Approach document reflects the definition set out in the Life Code.

Delays Caused by a Financial Firm – Page 4

The paragraph could be clearer, as it currently suggests an obligation broader than what is required under the Life Insurance Code of Practice (LICOP 6.18, 6.24, 6.25). It would also be useful if the references to fairness and reasonableness were aligned with commercial standards. For example, case law ties the duty of utmost good faith to standards of decency and fairness, considering both the insurer's and insured's interests. A similar link here would be beneficial.

Additionally, the paragraph should clarify that the information provided to the insurer should be enough to begin the assessment. The LICOP defines the 'Claim Received Date' as the date the insurer records receiving the first piece of information that allows them to start the claim assessment, even if not all information is received at that time. It would help to incorporate this definition for clarity.

The draft document also goes on to say:
"If insurers don't comply with these timeframes AFCA will expect them to provide compelling reasons"

We are concerned the drafting isn't consistent with the legal obligation under Section 57, which is a test of reasonableness. Creating an obligation to show "compelling" evidence could elevate that obligation. We therefore propose:
"If insurers don't comply with these timeframes AFCA will expect them to provide ~~compelling~~ reasons demonstrating the insurer's failure to make a payment earlier was not unreasonable in the circumstances".

Page 5

The section that reads:
"In determining the actual source of the delay AFCA will consider if any requests made by an insurer were reasonable. For example, AFCA may consider it reasonable for a complainant to refuse to attend a medico-legal examination if there is already sufficient evidence on the file for the insurer to make a decision."

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There are times when the evidence may appear to support the payment of a claim, but the insurer might still have genuine concerns for various reasons, leading them to seek an Independent Medical Examination (IME). The concern is that the draft wording could be misinterpreted as preventing the insurer from further investigating the evidence. With that in mind, we propose it could be amended to:

"In determining the actual source of the delay AFCA will consider if any requests made by an insurer were reasonable. For example, AFCA may consider it reasonable for a complainant to refuse to attend a medico-legal examination where the insurer has already commissioned prior IMEs and that evidence ~~if there is already~~ is sufficient evidence ~~on the file~~ for the insurer to make a decision."

By refining these sections, we hope to ensure both Approach documents support fair outcomes for all stakeholders. We value our collaborative relationship with AFCA and the ongoing dialogue to clarify these complex issues and hope to work together to resolve them in a way that is both practical and fair for all parties involved. We believe that open communication and a willingness to understand both the insurer's and AFCA's perspectives will help ensure we can continue providing the best possible outcomes for policyholders.

Thank you for the opportunity to contribute to this important discussion.

Kind regards,

Christine Cupitt
Chief Executive Office
Council of Australian Life Insurers