

# Life Insurance Code of Practice

Consultation draft released in November 2018

## **AFCA submission**

January 2019

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## Introduction

The Australian Financial Complaints Authority (AFCA) is the new independent external dispute resolution (EDR) scheme for the financial sector. It replaces the Financial Ombudsman Service (FOS), the Credit and Investments Ombudsman (CIO) and the Superannuation Complaints Tribunal (SCT).<sup>1</sup>

AFCA sees its purpose as providing fair, independent and effective solutions for financial disputes. It does this not only by providing fair dispute resolution services, but also by working with its members to improve their processes and drive up industry standards of service, thereby minimising disputes.

More broadly, AFCA will play a key role in restoring trust in the financial services sector.

In addition to providing fair, independent and effective solutions for financial disputes, AFCA has responsibilities<sup>2</sup> to identify, resolve and report on systemic issues and to notify the Australian Securities and Investments Commission (ASIC) of serious contraventions of the law, which go beyond individual dispute resolution.

On 1 May 2018, AFCA was authorised pursuant to the *Corporations Act 2001*. The AFCA Rules, which govern our operations, were approved by ASIC in September 2018. We began to receive complaints under these rules on 1 November 2018.

AFCA welcomes the opportunity to contribute to the development of the Life Insurance Code of Practice (Life Code) by providing feedback on the consultation draft released by the Financial Services Council on 12 November 2018 (Draft Code). This submission<sup>3</sup> draws on the experience of the predecessors of AFCA – organisations that have handled life insurance disputes for more than 25 years.

Key points in this submission are:

### Scope

We note that the Insurance in Superannuation Voluntary Code of Practice is to become Chapter 2 of the revised Life Code and is not subject to change.

AFCA considers that all code subscribers should comply with relevant provisions of the Life Code. It would be very confusing for consumers to have a code with some mandatory and some voluntary provisions and some subscribers whose compliance with the code's obligations was only voluntary.

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<sup>1</sup> Appendix 1 provides a brief overview of AFCA. For comprehensive information about AFCA, see our website [www.afca.org.au](http://www.afca.org.au).

<sup>2</sup> See [ASIC's Regulatory Guide 267](#) *Oversight of the Australian Financial Complaints Authority*.

<sup>3</sup> This submission has been prepared by the staff of AFCA and does not necessarily represent the views of individual directors of AFCA.

Currently there appear to be significant and competing differences between some of the obligations in Chapters 1 and 2. These should be reconciled to reduce duplication and competing obligations and to avoid confusion for consumers, code subscribers and code monitors alike.

### **Fairness**

The Life Code should impose an overarching obligation to treat consumers fairly in all circumstances. This obligation should be stated prominently and in broad terms to make clear that:

- fairness is the ultimate focus of the code
- the new obligation applies to all subscribers and parties acting for them.

### **Enforceability**

Transparent enforceability is key to stakeholder confidence in the Life Code and industry's commitment to it.

It has been unclear during the current consultation process whether the Chapter 2 provisions will be mandatory for all code subscribers and how the Life Insurance Code Compliance Committee will monitor and enforce these provisions. We encourage the FSC to address these matters quickly.

Consumers should be able to enforce obligations under the Life Code. To address this, AFCA suggests the code itself requires its provisions to form part of the contract between subscribers and consumers. Alternative approaches are to:

- state, in the Life Code, that subscribers are legally bound by the obligations in the code
- give the code the force of law by prescribing it under the *Competition and Consumer Act 2010*<sup>4</sup>
- seek approval of the code under ASIC's Regulatory Guide 183.

### **Key Code Promises**

The Life Code should make clear that its Key Code Promises have the same effect as other provisions imposing obligations in numbered sections of the code.

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<sup>4</sup> We confirm that the suggested change to enhance enforceability is required in addition to ASIC approval, which is suggested below.

## **ASIC approval**

The Life Code, when reviewed, should be suitable for approval by ASIC and submitted to ASIC for approval.

## **Principles**

The principles stated in section 1.7 of the Life Code should underpin enforceable obligations. Section 1.7 should operate either as a stand-alone obligation or in conjunction with specific obligations imposed elsewhere in the code, to guide their interpretation.

## **Conduct of distributors**

The Life Code should protect all consumers as consistently as possible, regardless of the distribution channels used. Following this approach, AFCA considers the code should make subscribers accountable for ensuring their distributors comply with the code.

## **Helping vulnerable people**

AFCA generally supports the proposed enhancements to the Life Code to improve engagement with vulnerable people. We consider that further measures are needed – particularly to assist people living with mental health conditions and indigenous people.

For example, we suggest the Life Code sets standards for reviewing and applying mental illness exclusions.

## **Medical definitions**

The Life Code should establish standard mechanisms, to apply to all life insurance policies, for reviewing, updating and interpreting medical definitions. The mechanisms should ensure definitions are easy to understand and keep up to date with community expectations and diagnostic practice.

The development of key fact sheets for standard terms such as severe rheumatoid arthritis, heart attack, stroke and cancer may assist consumers to better understand their insurance cover.

## **Assessment of claims**

The Life Code should ensure that, when claims are made, they are assessed appropriately, in a timely way, and not approached as investigations and reviews of underwriting decisions.

## Disclosure of premiums

The premium disclosure requirements in sections 3.4 and 3.6 of the Draft Code should be strengthened. AFCA suggests:

- enhanced requirements for stepped and level premiums
- new requirements to provide premium projections.

## Timeframes

Specific timeframes set in the Draft Code should be reviewed to ensure they operate fairly for consumers. Exceptions and exclusions should be kept to a minimum in provisions that set timeframes.

## Cancellation of policies

The Life Code should commit subscribers to complying with section 210 of the *Life Insurance Act 1995*.

We encourage industry to develop a standard notice for cancellation of a life insurance policy due to non-payment of premiums.

## 1. Scope

We note that the Insurance in Superannuation Voluntary Code of Practice is to become Chapter 2 of the revised Life Code and is not subject to change.

AFCA considers that all code subscribers should comply with all relevant provisions of the code. It would be very confusing for consumers to have a code with some mandatory and some voluntary provisions and some subscribers whose compliance with the code's obligations was also only voluntary.

Currently there are significant and competing differences between some of the obligations in Chapters 1 and 2. These should be reconciled to reduce duplication and competing obligations and to avoid confusion for consumers, code subscribers and code monitors alike.

ASIC's Regulatory Guide 183 addresses important issues including code coverage, adequacy of code provisions and multiple codes. While we appreciate there are technical challenges in establishing a single code given the different entities involved, we support the development of a single code that covers both life and group life insurance products. In our view, this is preferable to having multiple codes which adds unnecessary complexity for consumers and difficulties in ensuring consistent standards of conduct, behaviour and treatment of consumers across the life insurance and superannuation industries.

## 2. Fairness

The primary focus of the framework to self-regulate life insurance services in Australia should be the fair treatment of customers at all stages of what is an increasingly integrated product design, origination and distribution system. This would help ensure the needs of all consumers are met.

The Life Code refers to requirements to treat consumers fairly in its Key Code Promises and provisions such as section 1.7. Given the information highlighted by recent inquiries and reviews, AFCA suggests the code should now also impose an overarching obligation to treat consumers fairly. A prominent provision should impose the obligation on all subscribers and parties acting for them.

In the United Kingdom, authorised financial services firms are subject to Principles for Businesses<sup>5</sup> that mandate fairness and good conduct. These principles could be used as a drafting model for the new obligation that we suggest.<sup>6</sup>

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<sup>5</sup> The Principles for Businesses are set out in the Financial Conduct Authority's [Handbook](#).

<sup>6</sup> For further explanation, see [AFCA's submission](#) in October 2018 in response to the Interim Report of the current Royal Commission into financial services.

### 3. Enforceability

The Draft Code contains provisions to make Chapters 1 and 2 binding by enabling the Life Insurance Code Compliance Committee to enforce the code against subscribers.

It has been unclear during the current consultation process whether the Chapter 2 provisions will be mandatory for all code subscribers and how the Life Insurance Code Compliance Committee will monitor and enforce these provisions. We encourage the FSC to address these matters quickly.

AFCA considers that, in addition, the code's obligations should be legally binding on subscribers and enforceable by consumers as a contract term.

AFCA suggests the Life Code should state that the code forms part of the contracts between subscribers and consumers. Alternative approaches to enhance code enforceability are:

- state, in the code, that subscribers are legally bound by the obligations in the code or
- prescribe the code under the *Competition and Consumer Act 2010* so that it has the force of law and can be enforced against subscribers.<sup>7</sup>

If the Life Code is to be made enforceable by consumers against all code subscribers, several provisions in the Draft Code will need to be amended. For example, the provisions headed 'Legal Status of Chapter 1' should be reviewed.

In recent discussions about the Life Code, the FSC has suggested that AFCA will **enforce** the code in its determinations of consumer complaints. To clarify, AFCA will take the code's obligations into account in our decision making in our general division and our assessment of what is fair in all the circumstances of an individual complaint. This may or may not result in compensation being payable to a consumer. This is not the same as enforcement action for failure by a code subscriber to comply with the code's obligations.

Rule A14 of the [AFCA Rules](#) states our approach to decision making. For present purposes, rules A14.1 and A14.2 are most relevant.

A.14.1 When determining a Superannuation Complaint, the AFCA Decision Maker:

- a) may refer a question of law to the Federal Court in accordance with section 1054C of the Corporations Act; and
- b) must apply the approach specified in section 1055 of the Corporations Act.

A.14.2 When determining any other complaint, the AFCA Decision Maker must do what the AFCA Decision Maker considers is fair in all the circumstances having regard to:

- a) legal principles,

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<sup>7</sup> Paragraphs 2 and 3 of the new Banking Code of Practice could be used as a model.



- b) applicable industry codes or guidance,
- c) good industry practice and
- d) previous relevant Determinations of AFCA or Predecessor Schemes.

When deciding a complaint other than a Superannuation Complaint<sup>8</sup>, rule A14.2 requires AFCA to do what is fair in all the circumstances having regard to factors including good practice and applicable industry codes. The Life Code plays a role in these decisions where it applies or sets good industry practice standards.

The current Insurance in Superannuation Voluntary Code of Practice may be considered in our superannuation division. If that code is inserted as Chapter 2 of the Life Code, the obligations would also form part of the assessment of decisions under rule 14A.1.

In deciding whether a trustee has acted in the best interests of members or made a decision that is fair and reasonable, AFCA may consider whether the superannuation provider has acted consistently with any relevant industry code or best practice guidelines. It would put the matter beyond doubt however if code subscribers would commit to the obligations being legally binding.

Enforceability is key to confidence in the industry's commitment to comply with the Life Code's obligations. Making the code legally binding would also provide certainty and clarity to the industry and consumers.

## 4. Key Code Promises

The status of the Key Code Promises in the Draft Code is unclear. It creates doubt about whether the promises are enforceable or simply aspirational.

AFCA considers that the Key Code Promises should operate in the same way as the other provisions of the Life Code. Like those provisions, the promises should be enforceable and should be monitored by the Life Insurance Code Compliance Committee. We suggest consideration be given to including the Key Code Promises as a new numbered section of the code.

## 5. Principles

The principles stated in section 1.7 of the Life Code should underpin enforceable obligations. Section 1.7 should operate either as a stand-alone obligation or in conjunction with specific obligations imposed elsewhere in the code, to guide their interpretation.

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<sup>8</sup> 'Superannuation Complaint' and other terms used in the AFCA Rules are defined in Section E of the rules.

AFCA considers that section 1.7 should be amended to clarify how the principles apply – as the basis of obligations, or as factors to be considered when interpreting other obligations.

## 6. ASIC approval

AFCA considers that the Life Code, when reviewed, should be suitable for submission and submitted to ASIC for approval under its Regulatory Guide 183. ASIC approval would be a strong signal to consumers that they can have confidence in compliance with the code and its enforcement.

## 7. Conduct of distributors

The Life Code makes subscribers accountable for the conduct of their staff and authorised representatives. For example, in the Draft Code:

- section 2.2 requires subscribers to ensure their staff and authorised representatives comply with Chapter 1
- section 25.6 provides that a subscriber breaches the code if its staff or authorised representatives fail to comply with the code
- Key Code Promise 2 commits subscribers to monitoring practices of their staff and authorised representatives.

Subscribers do not appear to have the same level of accountability under the Draft Code for the conduct of their distributors. We acknowledge that sections 4.2B and 4.7 impose certain obligations on subscribers to promote code compliance by distributors. However, these obligations are limited, there is no equivalent of section 25.6 applying to breaches by distributors and the Key Code Promises do not include any commitment relating to practices of distributors.

In our view, the Life Code should protect all consumers as consistently as possible, regardless of the distribution channels used. Following this approach, AFCA considers that the Life Code should hold subscribers accountable for the distribution of their product and ensuring distributors and third-party agents comply with the code.

## 8. Helping vulnerable people

In our experience, people living with mental illness and mental health conditions are particularly affected by:

- their access to insurance products
- underwriting
- policy exclusions

- the handling and assessment of claims
- their ability to meet all requests for information or attendance at medical appointments
- surveillance and claim investigation activity
- treatment by insurers when they raise concerns about services provided.

In a determination of a dispute in 2017, FOS found that a blanket exclusion relating to mental illness was discriminatory and unlawful under the *Disability Discrimination Act 1992*. This determination<sup>9</sup>, which is published on AFCA’s website, provides further details.

We strongly support the inclusion of standards to prevent discriminatory conduct and behaviour in the provision of life insurance services and products.

## 9. Medical definitions

Public submissions made by FOS in recent years included detailed comments and recommendations about medical definitions.<sup>10</sup> These submissions reflect the views of AFCA. Our key points are noted below with observations about relevant provisions in the Draft Code.

- Definitions must be clear and easy to understand

We acknowledge that Appendix 1 has been added to the Life Code. However, we consider the definitions in the appendix are difficult to understand and strongly recommend that they are expressed more simply.

- New standards for definitions should apply to all policies

In the Draft Code, section 8.20A states that the definitions in Appendix 1 apply only in relation to particular products issued from July 2017 onwards.

The only requirement in the Draft Code to update definitions is imposed through section 3.2. This provision applies only to policies ‘available for new customers to buy’.

Footnote 5 imposes a limitation on section 3.2. It is not clear whether it only applies to the last sentence of section 3.2 or it states that section 3.2 does not apply at all to cover under group policies.

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<sup>9</sup> [Determination 428120](#).

<sup>10</sup> See submissions by FOS in [September 2016](#) on the Second Consultation Draft of the Life Code and in [November 2016](#) to the Inquiry into the Life Insurance Industry.

- Definitions should be kept up to date with community expectations and diagnostic practice

Section 3.2 sets a timeframe for reviews of definitions and requires ‘consultation with relevant medical specialists’. The Draft Code does include any further provisions to specify standards that reviews of definitions and resulting updates must meet. It does not deal with issues such as:

- > What evidence must reviews consider?
- > How must updates be made?

AFCA considers that the following measures would also help to ensure that medical definitions operate fairly:

- Developing key facts sheets about standard medical definitions.
- Including provisions in the Life Code to require insurers to regularly upgrade standard medical definitions and take into account section 54 of the *Insurance Contracts Act 1984*.
- Requiring the industry to report annually to the Life Insurance Code Compliance Committee on outcomes of medical definition reviews undertaken, numbers of policies affected, nature and type of amendments made to definitions and consultations undertaken.

## 10. Assessment of claims

AFCA’s complaint resolution experience indicates that most insurers commence consideration of larger life insurance claims with an investigation and review of the original underwriting decision, rather than the claim itself. That is inappropriate.

The proposed changes to the Life Code are helpful, but do not go far enough. For example, they do not prevent an insurer from requiring a complete set of doctor’s notes at the outset of the claim, which can then be used as justification for a review of the original underwriting decision.

AFCA recommends the wording of section 8.5A be amended to address this issue and prevent this conduct.

The Life Code does not currently require insurers to give claimants the material the insurer relied on to decline their claim. It is important that insurers can clearly explain not only the decision, but also the reasons for the decision.

Section 8.15 proceeds on the assumption that the insurer may, not must, provide such information. We strongly recommend section 8.19 be amended to address this matter to ensure that consumers have full disclosure of information on which decisions have been made.

## 11. Disclosure of premiums

AFCA receives many complaints about the clarity of premium and fee disclosure and the failure to adequately explain premium increases that may apply year on year. These complaints arise in relation to both stepped and level premiums.

AFCA strongly recommends that the premium disclosure requirements in sections 3.4 and 3.6 of the Draft Code be strengthened to reduce these types of complaints. These requirements are:

- for a 'Life Insurance Policy', to provide in plain language –
  - > information about how much your cover costs (the premiums) (s3.4c))
  - > a description of how the premiums you pay might change, for example whether regular premiums are stepped or level (s3.4h))
- for a 'Funeral Insurance Policy', more extensive obligations under section 3.6b), c) and i) including obligations to provide illustrations (s3.4c) and i)).

### Stepped premiums

AFCA sees many complaints where consumers are surprised by the rate at which their stepped premiums increased over time.

ASIC recently reviewed the sale of direct life insurance and found that none of the insurers reviewed provided clear information about the future cost of insurance policies.<sup>11</sup> Life insurance is a product for the long term. It is unacceptable for consumers to be sold life insurance without clear expectations of what it is likely to cost over the long term.

To address this serious problem, we recommend the Life Code mandate that insurers give consumers an estimate (expressed graphically and in numbers) of how much stepped premiums will cost per year over the life of the policy. After the sale, that estimate should be updated and provided with each renewal notice.

### Level premiums

AFCA also sees many complaints from policy holders who are surprised that level premiums have increased sometimes substantially and often, because of premium re-rates. AFCA acknowledges APRA's concerns about the viability of some sections of the life insurance market, and the need for insurers to retain the right to re-rate. However, the label 'level premiums' seems to create a false impression with consumers that the premiums will remain the same for the life of the policy.

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<sup>11</sup> See [ASIC's Report 587](#) *The sale of direct life Insurance*, released on 30 August 2018.

Unfortunately, we have also seen instances where premium increases have not been adequately explained even to us. Insurers cannot exercise discretion indiscriminately.

At the very least, consumers should be provided with a statement about the likelihood that premiums may increase year on year.

### **Illustrations**

Section 3.6 requires disclosure material for Funeral Insurance Policies to include illustrations of how future premiums might increase. In our view, these requirements are insufficient.

A consumer buying a long-term product like life insurance needs to know how much it is likely to cost not just in the first year, but in each year over the life of the policy. AFCA considers that the Life Code should require a projection of premiums – expressed graphically and in numbers - over the life of the policy.

We acknowledge the difficulties some insurers may have in providing premium projections with current systems. This however should not relieve insurers of the obligation to provide information essential to informed decisions when purchasing insurance. Insurers have rates tables for example that could be adapted for this purpose.

## **12. Timeframes**

### **Commencement of timeframes**

Delay in claims and complaints handling is unfortunately a regular recurring theme in life insurance disputes. Delays cause significant stress and anxiety at what is already a difficult time for consumers.

Certain timeframes specified in the Draft Code may not commence until a consumer has already encountered long delays. For example, time does not start to run against a subscriber under sections 8.15 and 8.21 until they obtain all the information they need to make a decision.

AFCA suggests a review of provisions for commencement of timeframes to ensure they operate fairly for consumers. Claims and complaint handling must be undertaken in a timelier manner going forward. The Life Code's timelines for the delivery of these services must be clear and mandatory, with as few exceptions as possible.

### **Unexpected circumstances**

The timeframes specified in sections 8.16 and 8.17 refer to 'Unexpected Circumstances'. These are given a broad definition in section 27. AFCA considers

that paragraph b) of this definition should be reviewed to ensure total and permanent disability claims are handled efficiently and in a timely manner.

The timeframe where 'Unexpected Circumstances' exist in section 8.17 has been altered, but the alteration is not highlighted, in the Draft Code. This appears to make the timeframe longer than it is in the Life Code at present. We consider that, in further consultation, this alteration should be highlighted and explained and stakeholders should be given an opportunity to comment on it.

### 13. Cancellation of policies

In consultations conducted when the Life Code was being developed, FOS explained its concerns about industry non-compliance with section 210 of the *Life Insurance Act 1995*. To improve compliance, FOS recommended the development of a standard form for any cancellation of a life insurance policy due to non-payment of premiums. AFCA considers this change is necessary at a minimum.

Our view is that in the absence of a regulatory or legislative change:

- The Life Code should state that a life insurance policy will not be cancelled due to non-payment of premiums unless the requirements of section 210 are met.
- The code should require use of a standard form to meet the notice requirements imposed by section 210.
- The form should comply with section 210 and specify in clear terms –
  - > the amount of the premium
  - > the date when the premium became payable
  - > the consequences of non-payment of the premium by the due date
  - > the amount that is required to be paid and by when.

### 14. Drafting matter

Several references to EDR in the Draft Code use historical terms that were used by FOS but are no longer used by AFCA. Examples are:

- 'dispute' in section 2.14 (now 'complaint' for AFCA)
- 'Terms of Reference' in sections 9.14 and 9.16 (now 'AFCA Rules').

## Appendix 1 – About AFCA

AFCA is a free, fair and independent dispute resolution scheme. AFCA's service is offered as an alternative to tribunals and courts to resolve complaints consumers and small businesses have with their financial firms. We consider complaints about:

- credit, finance and loans
- insurance
- banking deposits and payments
- investments and financial advice
- superannuation.

AFCA's role is to assist consumers and small businesses to reach agreements with financial firms about how to resolve their complaints. We are impartial and independent. We do not act for either party to advocate their position. If a complaint does not resolve between the parties, we will decide an appropriate outcome.

Decisions made by AFCA can be binding on the financial firm involved in a complaint. We can award compensation for losses suffered because of a financial firm's error or inappropriate conduct. There are other remedies we can also provide for superannuation complaints. We do not, however, award compensation to punish financial firms or impose fines.

AFCA is not a government department or agency, and is not a regulator of the financial services industry. We are a not-for-profit company, limited by guarantee, governed by a board with equal numbers of industry and consumer representatives. AFCA's Chief Ombudsman is responsible for the management of the organisation.

Under transitional arrangements that have been put in place with ASIC's approval, AFCA is currently resolving complaints made to FOS and CIO and will continue to do so until they are resolved. These complaints will be handled in accordance with the FOS Terms of Reference or CIO Rules, as applicable and in force when the relevant complaint was lodged.

AFCA is built upon the work of FOS, CIO and SCT.<sup>12</sup> However, in time, AFCA will develop new approaches informed, but not bound, by those predecessor schemes' approaches to resolving disputes.

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<sup>12</sup> A joint working group headed by Dr Malcom Edey was established and the schemes collaborated to develop AFCA and integrate the superannuation jurisdiction.