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Dear Mr Spear

Reforms to the sale of add-on insurance products – Proposal Paper

Our organisations welcome the opportunity to comment on The Treasury's *Reforms to the sale of add-on insurance: Proposal Paper*, 9 September 2019 (**Proposal Paper**).¹ The following consumer organisations have contributed to and endorsed this submission:

- Consumer Action Law Centre
- Financial Rights Legal Centre
- Consumer Credit Legal Service WA

Further information about the contributors is available at **Appendix A**.

Executive summary

Consumer advocates have held long-standing concerns about the sale of junk add-on insurance and worthless extended warranties in car yards, banks, and retail stores. It is irrefutable that the add-on insurance market is failing consumers, producing significant harm and in dire need of oversight and reform.

Insurance is a complex – and sometimes worthless – product. It cannot be safely sold when added on at the tail-end of purchasing of a car, home, loan, mobile phone, ticket or pet. People need time and meaningful information to assess their need for insurance, compare deals, understand complex policy terms, and make their own decision, free from the high-pressure sales environment fuelled by commissions. Known behavioural biases inherent in the add-on sales process have been long exploited by the insurance industry – and their retailing partners – that has prioritised making a quick buck over selling suitable insurance products that people want and need.

¹ Information about this consultation is available at: <https://treasury.gov.au/consultation/c2019-t408984>.

This harmful sales practice, together with conflicted remuneration and poor product design, has led to the estimated \$1 billion clean-up bill for the multi-decade scandal of junk add-on insurance. Similar scandals in the United Kingdom are estimated to reach £53 billion.²

Since 2016, Consumer Action's free tool [DemandaRefund.com](https://www.demandarefund.com) has helped people to demand over approximately \$5.18 million in refunds for junk consumer credit insurance (CCI), guaranteed asset protection (GAP) insurance and worthless extended warranties sold by car yards, insurers, lenders and warranty providers and lenders. The results from an empirical analysis of the recorded 1,950 demands for a refund on CCI are shocking but unsurprising given the inherent problems in the dynamics of add-on sales:

- 97% of users did not think that the salesperson had explained all the important exclusions and limitations;
- 52% felt pressured by the salesperson into buying the insurance;
- 88% did not think that the sales process was fair;
- 39% didn't even know they had bought the insurance; and
- most damning of all, not a single person responded that they would have bought the insurance, knowing what they know now.³

To stop the ongoing harm and prevent any repetition of this sorry chapter in our financial services history, we must implement an effective deferred sales model. A robust deferred sales model would prevent salespeople from being able to bundle junk insurance in with the sale of a primary product, by requiring a break in the sale process. This break is critical, as it gives consumers time to assess the value of the additional product at a separate time, rather than being simultaneously sold extra products in a high-pressure sales environment where consumers are focused on the purchase of the main product such as a car, loan or phone.

We strongly support the Government's commitment to implement Recommendation 4.3 of the Final Report of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry (FSRC):

A Treasury-led working group should develop an industry-wide deferred sales model for the sale of any add-on insurance products (except policies of comprehensive motor insurance). The model should be implemented as soon as is reasonably practicable.⁴

While we broadly support the intent of the proposed model and the Government's swift implementation, we hold serious concerns about elements of the model. Our primary concerns are:

- **The trigger for the deferral period being a 'financial commitment':** The deferral period must start after the primary good or service has been purchased, financed *and* delivered to prevent the collection of the good, or signing of the loan contract, being used as a high pressure sale of junk add-ons, which would defeat the very purpose of the reform.
- **The one-day 'customer initiated' completion of sale:** This is open to abuse by retailers, who can simply pressure people into calling up the next day to get the purported discount or deal. This proposal is particularly risky when combined with the current proposed trigger event of an application for finance

² BBC News, *Industry bill for PPI claims could hit £53bn*, 5 September 2019, accessed 30 September 2019: <https://www.bbc.com/news/business-49592643>.

³ For more analysis, see pages 14-16 of this submission.

⁴ Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry, *Final Report*, 1 February 2019.

because consumers may feel pressured to follow the salesperson's suggestion in order to secure finance. This proposal creates a huge loophole that is inconsistent with Commissioner Hayne's recommendation that loopholes be minimised. It should be removed from the final model.

- **The duration of the deferral period:** This should be extended to a minimum of seven days, as recommended by the Productivity Commission.
- **Exemptions:** Any exemption from the deferred sales model provided by the Australian Securities and Investments Commission (**ASIC**) should be time-limited and apply at the individual product level, not the product category level. Criteria for exemptions should include: a claims ratio of 90% (consistent with comprehensive car insurance), to ensure the product is good value; and a ban on conflicted remuneration.
- **Tiered design:** The three-tier design is overly complex and subject to the limitations of the Product Intervention Power (**PIP**). We recommend that the deferred sales model apply economy wide, unless modified by a Product Intervention Order.

We note that it is difficult to comment on the effectiveness of the PIP as an intervention for the most egregious add-on products in the absence of proposed uses of the PIP. We have not had the opportunity to review in detail ASIC Consultation Paper 324, *Product intervention: The sale of add-on financial products through car yard intermediaries*,⁵ but a cursory review reveals significant limitations. For example, the trigger event will be a commitment to purchase or acquire a particular vehicle, including an application for finance. This will clearly be open to abuse by car dealers as the consumer may need to re-engage with the salesperson to take possession of the car or sign the loan contract, putting them at risk of a high-pressure sale of junk insurance – again undermining the very intent of the reform.

If the tiered design remains, we recommend that the following products be subject to the following tiers:

- **Tier One (Product Intervention Order):**
 - Consumer credit insurance;
 - Guaranteed asset protection insurance;
 - Loan termination insurance;
 - Tyre and rim insurance;
 - Mechanical breakdown insurance and extended warranties, including “dealer-issued” warranties and warranties provided in retail stores.
 - These interventions should apply across all sales channels, including car yards, banks and credit unions, and retailers. Subject to further investigation by ASIC, other add-on products may belong in this tier. For example, we hold concerns about the value and sales of ticket insurance, travel insurance, phone handset insurance and pet insurance.
- **Tier Three (Exemption):** Individual policies of comprehensive car insurance that meet the additional claims and commissions criteria we recommend.

⁵ 1 October 2019: <https://asic.gov.au/about-asic/news-centre/find-a-media-release/2019-releases/19-267mr-asic-consults-on-reforms-to-sale-of-add-on-financial-products-sold-with-cars>.

- **Tier Two (Deferred Sales Model):** All other add-on insurance, including travel, ticket, and phone handset insurances.

Our experience speaking to consumers on a daily basis is that the problems investigated and proven to be found with respect to add-on insurance in car yards equally apply to most, if not every other form of add-on insurance. For example, the deferred sales model should apply to add-on travel insurance to give people time to consider their insurance needs and the complex conditions, benefits and tricky exclusions in the policy, away from pressure-sales dynamics fuelled by commissions. It is critical that travellers get an insurance policy that is suitable for their needs – too often people face shocking outcomes when a claim is denied due to an exclusion. The risk of underinsurance is very low, as most travel insurance is arranged 88 days before departure.⁶ A wide range of methods are used to arrange travel insurance, with 31% of people buying direct from the insurer, so anyone who wants or needs travel insurance can get it immediately through other channels, and likely for a better price.

This submission also comments on the following issues:

- The need for ASIC to commence investigations into all remaining add-on product lines;
- Conditions that should be placed on exemptions;
- The need to prevent 'bridging' insurance; and
- The interaction with ban on unsolicited selling of insurance.

We note that both Commissioner Hayne⁷ and the Productivity Commission⁸ recommended that the Australian government should establish a 'Treasury-led working group to develop an industry wide deferred sales model for add-on insurance'. We are not aware of consumer groups being involved in any working group led by Treasury. This is in contrast to the working groups led by ASIC in 2016 on add-on insurance sold through car yards. In light of the lack of a working group with direct input from consumer advocacy organisations that have worked at the forefront of this problem for many years, this submission comments on issues necessary for an effective implementation of an economy-wide deferred sales model.

We strongly encourage Treasury to adopt our recommendations, listed below, in the final model. Otherwise, we fear that this reform will not fix the problem of add-on insurance, and will not meet the expectations of Commissioner Hayne, or Australians who are sick of being mis-sold junk add-on insurance.

⁶ Quantum Market Research, *Survey of Australians' Travel Insurance Behaviour*, Prepared for the Insurance Council of Australia and the Department of Foreign Affairs and Trade, August 2016, page 27: <https://smartraveller.gov.au/guide/all-travellers/insurance/Documents/survey-travel-insurance-behaviour-web.pdf>.

⁷ Final Report, above n 4, Recommendation 4.3.

⁸ Productivity Commission, *Competition in the Australian Financial System: Inquiry Report*, 28 June 2018 (**Competition Report**), Recommendation 15.1, page 432: <https://www.pc.gov.au/inquiries/completed/financial-system/report>.

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Summary of Recommendations

RECOMMENDATION 1. Modify the design of the deferred sales model so that:

- a) a legislated deferred sales model applies economy-wide to all add-on products;
- b) ASIC may use the product intervention power (**PIP**) on products to augment the legislated deferred sales model as required, for example by extending the deferral period or banning the the add-on product or distributed model outright; and
- c) ASIC may provide, in extremely limited cases meeting set criteria, an exemption at the individual product level.

RECOMMENDATION 2. Criteria for exemption from the deferred sales model should include that:

- a) the product meets a historical and ongoing claims ratio of at least 90%.
- b) the product issuer (i.e. the insurer) is not paying conflicted remuneration to the retailer or distributor (i.e the car dealer).

RECOMMENDATION 3. Exemptions should be time-limited to ensure the product continues to meet the criteria.

RECOMMENDATION 4. To ensure good consumer outcomes, any exemption from the deferred sales model provided by ASIC should come with the following conditions:

- a) consumers be clearly informed that they do not have to purchase the insurance from the salesperson/primary product provider;
- b) information about alternative products/options is provided;
- c) a mechanism is in place to ensure that consumers can obtain these alternative insurances as simply and easily as at the point of sale of the primary product;
- d) any insurance purchase cannot be financed;
- e) a cooling-off period of 21 days or longer is provided, and in the case of travel insurance where exercising cooling off periods often mean no refund on premiums once a journey has commenced, give particular regard to how this is worded and explained.

RECOMMENDATION 5. ASIC should immediately commence investigations into all add-on insurance products that have not previously been subject to detailed scrutiny to identify further products that should be subject to the PIP.

RECOMMENDATION 6. At a minimum, the following products should be subject to a Product Intervention Order (Tier One):

- a) Consumer credit insurance
- b) Guaranteed asset protection insurance
- c) Loan termination insurance
- d) Tyre and rim insurance
- e) Mechanical breakdown insurance and extended warranties, including “dealer-issued” warranties.

RECOMMENDATION 7. The sale and distribution of mechanical breakdown insurance and warranties should be regulated under a model that prohibits the sale of these products more than one month before the expiry of the manufacturer's warranty.

RECOMMENDATION 8. ASIC should seek clarity in relation to whether or not dealer warranties fall within the Corporations Act exemptions.

RECOMMENDATION 9. Subject to Recommendations 2 to 4, comprehensive car insurance policies should be eligible to apply to ASIC for an exemption from the deferred sales model (Tier Three).

RECOMMENDATION 10. All other insurance products sold as an add-on to a primary product or service should be sold via a deferred sales model (Tier Two).

RECOMMENDATION 11. The deferral period should only begin once the primary good or service has been purchased, financed *and* delivered to the consumer, and the prescribed information has been provided.

RECOMMENDATION 12. Innovative, interactive consumer communication techniques should be mandated and supervised to ensure greater consumer understanding and purchase of suitable add-on insurance products. To ensure this, we support a standardised model that is active/interactive and not passive (that is simply providing a piece of paper); and includes a series of 'filter' or 'knock out' questions, before the purchase of the product.

RECOMMENDATION 13. Extend the deferral period to a minimum of seven days from the trigger event.

RECOMMENDATION 14. Remove the customer-initiated completion of sale from the deferred sales model for add-on insurance.

RECOMMENDATION 15. The final model should include consumer remedies for breach of the deferred sales model. Remedies should be sufficient to put the consumer back in the position they would have been in and to deter breaches.

RECOMMENDATION 16. Remediation schemes should be designed at the same time as monitoring and compliance systems.

RECOMMENDATION 17. The commencement of the deferred sales model should be a maximum of 12 months, and ideally 6 months or less, from passage of the legislation.

RECOMMENDATION 18. The legislation should ensure that there is no ability to undertake regulatory arbitrage with the creation of 'bridging' insurance during the deferral period.

RECOMMENDATION 19. Insurers should reduce or remove waiting periods altogether in add-on products to reduce the period in which consumers are uninsured.

Request for feedback 1: Please provide evidence as to why a particular type of add-on insurance product should reside in a particular tier

Tier design

In order to respond to Treasury request for feedback on which products belong in which tiers, it is first necessary to comment on the tier design. The Proposals Paper proposed a three-tier model:

Tier	Description of add-on insurance product by tier	Proposed treatment under legislation
1	Products causing significant consumer detriment	ASIC Product Intervention Power
2	Default tier for all add-on insurance products (not in tiers one and three)	Legislated deferred sales model
3	Case-by-case exemptions for products that meet relevant criteria	Legislated ASIC exemptions power

We strongly support an economy-wide deferred sales model for all add-on insurance and accept that different add-on products may require different treatment. However, we have two concerns that require a small modification to the design. Below we propose an Alternative Design that would address our concerns while maintaining consistency with Treasury’s intentions and FSRC Recommendation 4.3.

Concern: Limitations of the Product Intervention Power

In principle, we support the use of the PIP to make effective and comprehensive interventions where add-on insurance is causing or likely to cause ‘significant consumer detriment’, depending on the particular use of the PIP.

However, the success of the proposed Tier One as a regulatory fix for the most egregious add-on insurance products is wholly dependent on the limitations of the PIP. That is, an intervention order made by ASIC using the PIP can only continue for the prescribed period (up to 18 months) unless the period is extended by ASIC with the approval of the Minister, following a report to the Minister from ASIC on whether the extension should be made. Further, if a court makes an order staying or otherwise affecting the operation or enforcement of an intervention order, the period of the court’s order is not included towards the prescribed period.

We note that CIGNO, a short-term credit provider that has long-concerned consumer groups, has just sought judicial review of ASIC’s decision to make the short-term credit product intervention order.⁹

It is therefore unlikely but possible that the intervention for the worst add-on insurance products could be overturned by a Minister (and therefore subject to lobbying efforts) or due to court action – while other less egregious add-on insurance products are subject to the Tier 2 deferred sales model. This means there may be a period where there is no deferred sales model applying to egregious add-on products. In that possible scenario, we would prefer that the Tier 2 legislated deferred sales model apply in the interim until modified by a product intervention order.

Regardless of the final model for reforming the sale of add-on insurance products, the Government may need to reconsider how the PIP works and develop permanent intervention orders in line with the approach in the United Kingdom.

⁹ <https://asic.gov.au/about-asic/news-centre/find-a-media-release/2019-releases/19-264mr-cigno-seeks-judicial-review-of-asic-decision-to-make-short-term-credit-product-intervention-order/>.

Concern: Exemptions should be at an individual product level

We support ASIC being the relevant body empowered to provide an exemption from the legislated deferred sales model.

However, we have concerns about Tier Three exemptions applying at the product category level rather than to individual products. Providing category-level exemptions does not distinguish between good and poor value products within the category, or incentivise better product design to achieve an exemption. There is a real issue with using the blunt method to contort entire sectors in a single tier. The criteria for an exemption must be on an individual product design level that insurance companies must meet.

We agree with the Proposals Paper that exemptions should only arise when there is 'strong quantitative evidence of product value and consumer understanding'. The difficulty is that product value can vary wildly even within a product category due to the policy terms (for example, the conditions, benefits, exclusions) and claims outcomes of particular policies.

Travel insurance is an exemplar of why the proposed Tier Three design needs reworking. CHOICE reviews have found there are great value, recommended travel insurance products, and then there are some that are complete duds, which offer minimal value and have onerous terms.

There is also the possibility of future add-on products being crafted to avoid falling in between the tiers. Fixing categories for exemption now creates the prospect of regulatory arbitrage, which has been a long-standing feature of this industry. One can imagine a product called "comprehensive car insurance" with in-built GAP insurance. As the Productivity Commission observed, cited with approval by Commissioner Hayne:

the regulatory paradigm appears to involve ASIC in a game of whack-a-mole with insurers and their retailing partners. Legislators cannot expect the regulator to be effective in this game.¹⁰

Alternative Design

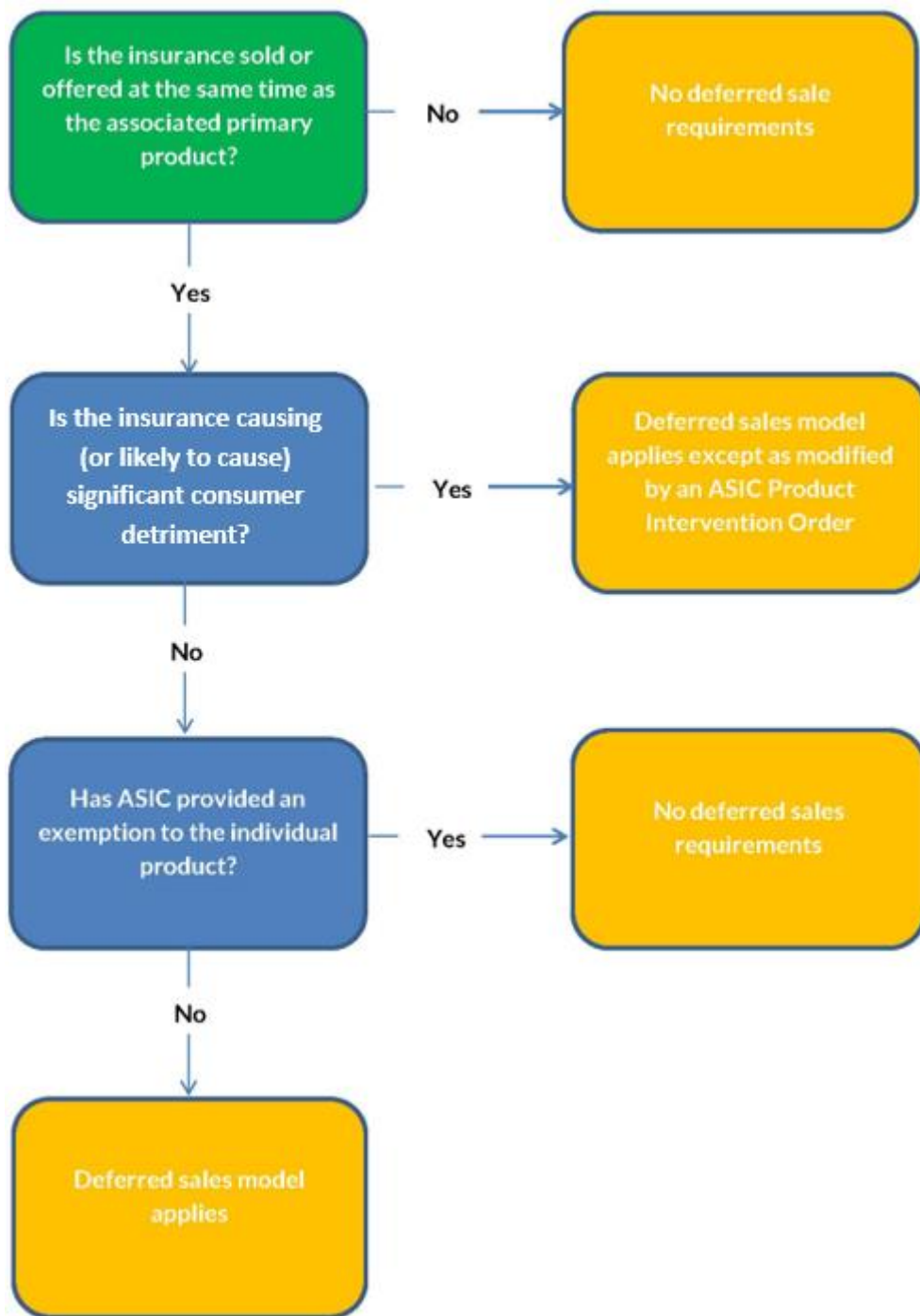
We propose an Alternative Design to slightly modify the model:

- A legislated deferred sales model applies economy-wide to all add-on insurance.
- ASIC should use the product intervention power (**PIP**) on products to modify the legislated deferred sales model as required, for example by extending the deferral period or banning the add-on product or distributed model outright.
- ASIC may provide, in extremely limited cases meeting set criteria, an exemption at the individual product level (subject to set criteria and conditions, discussed below at pages 13-14).

Under our Alternative Design, Figure 1 in the Proposals Paper would read as follows

¹⁰ Productivity Commission, Competition Report, above n 8, page 430.

Figure 1 Overview of alternative tiered deferred sales model



Benefits of our Alternative Design:

- **Consistency** with FSRC Recommendation 4.3 and the intention of Treasury's proposed model but avoids the concerns above.
- **Reduces the risk of regulatory arbitrage:** Depending on the final legislative drafting, it is possible that canny providers create products that fall between the categories of add-on insurance in the legislated model but are outside the scope of any product intervention orders. Similarly, it would prevent the creation of poor value 'comprehensive car insurance' policies or other poor value policies that are crafted to fall within product category exemptions.

- **Future-proof:** In any event, ASIC may need to use the PIP on products in the legislated deferred sales model. For example, there may be products in Tier Two or Three today that in future cause significant consumer detriment necessitating use of the PIP. Ticket cancellation insurance is one potential product. In that eventuality, ASIC would need to use the PIP on top of the legislated deferred sales model and modify its requirements to stop the consumer harm. Our design creates flexibility in the model, rather than setting categories now that may not reflect the consumer outcomes for particular products in future.
- **Incentivises a 'race to the top':** Encourages insurers and retailers within a product category to develop, for example, valuable comprehensive car insurance policies that meet the criteria for exemption.
- **Simpler and easier to convey to consumers:** The deferred sales model would be economy-wide, unless modified by an ASIC product intervention order or exemption.

RECOMMENDATION 1. Modify the design of the deferred sales model so that:

- a) A legislated deferred sales model applies economy-wide to all add-on products;
- b) ASIC may use the product intervention power (**PIP**) on products to augment the legislated deferred sales model as required, for example by extending the deferral period or banning the the add-on product or distributed model outright; and
- c) ASIC may provide, in extremely limited cases meeting set criteria, an exemption at the individual product level.

Criteria for exemption

We agree that there should be set criteria for an exemption. Exemptions should be time-limited to ensure the product continues to meet the criteria.

'Historically good value for money'

This criterion is vague and open to interpretation and would be better expressed as a particular claims ratio. Claims ratios are one of the most effective measures of product value, as it describes the average amount returned to consumers as a percentage of premiums paid. In supporting an exemption for comprehensive car insurance, Commissioner Hayne cited¹¹ the Productivity Commission views that comprehensive car insurance product rates among the highest value to consumers as measured by the share premiums returned in claims and content claims acceptance rates.¹²

We recommend a claims ratio of 90% as a criterion for exemption. This is based on the comprehensive car insurance claims ratio of 89%,¹³ and therefore consistent with the recommendations of Commissioner Hayne and the Productivity Commission.

'Well understood by consumers'

We have yet to see an insurance policy that that is well-understood by the majority, if any, of consumers due to the myriad of known problems with product design, product comparison and disclosure. This criterion is unlikely

¹¹ Final Report Vol 1, above n 4, at page 290.

¹² Productivity Commission, Competition Report, above n 8, page 430.

¹³ ASIC, Consultation Paper 324, *Product Intervention Power: The sale of add-on financial products through caryard intermediaries*, October 2019, para 23; see also the Productivity Commission's analysis of claims ratios between 2012 and 2018, which ranged between 83-98%, above n 8, at Figure 14.6 and page 415.

to be an effective consumer protection measure alone without further reforms to standard cover, key terms, and disclosure in general insurance.

Commissions

Much of the harm and impetus to mis-sell add-on insurance has come from the astronomical commissions paid by insurers to distributors to push a particular product. In addition to motivating mis-selling, commissions increase the cost of the insurance to the consumer dramatically, which is a poor and unfair outcome.

ASIC's extensive work found shocking outcomes driven by commissions, where car dealers received four times more in upfront commissions than consumers received in claims.¹⁴ As ASIC states, conflicted remuneration has resulted in poor consumer outcomes through:

- a. 'reverse competition' as illustrated by the add-on insurance market where insurers were competing for access to car dealer networks to sell their products, which led to dealers demanding higher payments or commissions, driving up the cost to consumers and eroding the value offered by their products;
- b. 'first mover' problems, where a single entity cannot move to fairer remuneration practices because they will lose business to their competitors; and
- c. driving sales of low-value products, especially under general advice models.¹⁵

These problems have also been found by the Productivity Commission, which observed that add-on insurance sold by product retailer serves to 'lock out competition from other insurers.'¹⁶

The problem is not unique to car yards. As the Proposals Paper notes, commissions paid on add-on travel insurance can be up to 65% of gross written premiums.

If, as expected, the junk insurance rort in car yards is finally cleaned up through a deferred sales model and other reforms, car dealers will be looking to other ways to supplement their income. Car dealers have been permitted to become dependent on revenue from add-ons.¹⁷ We are concerned that dealers may seek to supplement income by demanding increased commissions for the sale of add-on comprehensive car insurance, which would be a poor outcome for consumers. To prevent this harm, an additional criterion for exemption should be added: no commissions payable by the insurer to the intermediary.

This would also bring the implementation of this reform into line with FSRC Recommendation 2.6 to review the exemption for general and consumer credit insurance from the ban on conflicted remuneration laws.

RECOMMENDATION 2. Criteria for exemption from the deferred sales model should include that:

- a) The product meets a historical and ongoing claims ratio of at least 90%.
- b) The product issuer (i.e. the insurer) is not paying conflicted remuneration to the retailer or distributor (i.e the car dealer).

RECOMMENDATION 3. Exemptions should be time-limited to ensure the product continues to meet the criteria.

¹⁴ ASIC, Report 492, *A market that is failing consumers: The sale of add-on insurance through car dealers*, September 2016, para 20.

¹⁵ ASIC, Submission to FSRC, *Round 6: Insurance*, 25 October 2018, para 51:

https://financialservices.royalcommission.gov.au/Submissions/Documents/Round-6-written-submissions/POL_9006_0001_0192.pdf.

¹⁶ Productivity Commission, *Competition Report*, above n 8, page 419.

¹⁷ ASIC, Consultation Paper 294, *The sale of add-on insurance and warranties through caryard intermediaries*, 24 August 2017, para 27; see also Australian Automotive Dealer Association, Submission to the Australian Competition and Consumer Commission, *New car retailing industry market study*, 21 November 2016, para 4.1.3.

Conditions on exemption

To ensure good consumer outcomes, we recommend that conditions be placed on any exemption granted by ASIC. Consumer understanding does not mean that it is easy to compare products at the point of sale, or that the product is necessarily of 'good value'. Even where the product may be of 'good value' when first sold, often as a loss leader, the loyalty tax may apply where premiums on car or home and contents insurance jump up dramatically at renewal time.¹⁸ As the Productivity Commission found, the retailer distribution channel does not provide consumers with adequate capacity to compare different products such as the cost of an add-on product sold by one dealership to the same or similar products sold by another dealership.¹⁹ This gives insurers and product retailers that sell add-on insurance price setting power.

RECOMMENDATION 4. To ensure good consumer outcomes, any exemption from the deferred sales model provided by ASIC should come with the following conditions:

- a) Consumers are clearly informed that they do not have to purchase the insurance from the salesperson/primary product provider;
- b) Information about alternative products/options is provided;
- c) A mechanism is in place to ensure that consumers can obtain these alternative insurances as simply and easily as at the point of sale of the primary product;
- d) Any insurance purchase cannot be financed;
- e) A cooling-off period of 21 days or longer is provided, and in the case of travel insurance where exercising cooling off periods often mean no refund on premiums once a journey has commenced, give particular regard to how this is worded and explained.

Which products belong in which tier?

ASIC investigations into all add-on insurance

ASIC should immediately begin a program of investigation into every category of add-on insurance. The General Insurance Code Governance Committee identified 28 add-on products,²⁰ but the focus of ASIC's investigations to date has been in the context of car yards and banks. There are likely to be egregious add-on products throughout this sector and it is incumbent upon ASIC to investigate and evidence this, particularly where the PIP is part of the model for implementation of this reform. Our experience speaking to consumers on a daily basis is that the problems investigated and proven to be found with respect to add-on insurance in car yards equally apply to most, if not every other form of add-on insurance or extended warranty.

A data collection program similar to life insurance²¹ should be implemented for all general insurance including add-on insurance to identify claims ratios and other information that will lead to identifying good and bad add-on products.

¹⁸ For more information on the 'loyalty tax' in insurance, see Consumer Action, Submission to the NSW Emergency Services Levy Insurance Monitor, *Discussion Paper: Pricing Differences: New vs Existing Customers*, 20 December 2018: <https://consumeraction.org.au/insurance-pricing-differences-new-vs-existing-customers/>.

¹⁹ Productivity Commission, Competition Report, above n 8, page 421

²⁰ General Insurance Code Governance Committee, *Who is selling insurance? 2014 General Insurance Code of Practice Own Motion Inquiry*, June 2018, page 28: [http://codeofpractice.com.au/assets/CGC%20REPORT/CGC%20report%20-%20Who%20is%20selling%20insurance%20\(18062018\).pdf](http://codeofpractice.com.au/assets/CGC%20REPORT/CGC%20report%20-%20Who%20is%20selling%20insurance%20(18062018).pdf).

²¹ <https://asic.gov.au/about-asic/news-centre/find-a-media-release/2019-releases/19-16omr-apra-and-asic-publish-latest-data-on-life-insurance-claims-and-disputes/>.

RECOMMENDATION 5. ASIC should immediately commence investigations into all add-on insurance products that have not previously been subject to detailed scrutiny to identify further products that should be subject to the PIP.

Tier 1: Products that should be subject to the Product Intervention Order

At a minimum, the following products at a minimum should reside in Tier One and be subject to a Product Intervention Order, regardless of distribution channel:

- Consumer credit insurance
- Guaranteed asset protection insurance
- Loan termination insurance
- Tyre and rim insurance
- Mechanical breakdown insurance
- Extended warranties, including non-insurance “dealer-issued” warranties

It abundantly clear that the add-on insurance market for the above products is failing consumers, producing significant harm and in dire need for oversight and reform. There is overwhelming, incontrovertible evidence of the need for the PIP to be used on the above products, including in:

- evidence to the Financial Services Royal Commission;
- ASIC Reports 256, 470, 471, 492, 622, and as summarised in Consultation Paper 294;
- sector-wide remediation schemes for mis-selling;
- reports of code monitoring committees, parliamentary committees and the Productivity Commission’s inquiry into Competition in the Australian Financial System; and
- importantly, the countless stories of people affected by this scandal over many decades, whether shared directly or via consumer organisations through our casework, case studies, and DemandARefund.com.

The particular intervention required may vary from product to product. For example, we agree with ASIC that tyre and rim insurance should not be sold because, with an average claim of \$334, consumers are better off self-insuring.²²

To prevent regulatory arbitrage, the intervention must apply across all distribution channels, including online. It should apply across all sales channels where intermediaries regularly arrange finance for cars, including car dealers, finance brokers and salary packaging firms. It should apply to extended warranties sold by retailers for consumer goods. In the interests of brevity, we will not repeat the above evidence on a known problem here and seek only to add new data. However, should it be needed, we would be happy to provide further submissions to The Treasury on why these products are so egregious as to warrant inclusion in Tier One.

Empirical analysis from DemandARefund.com

Consumer Action’s Demandarefund.com continues to see considerable traffic from people aggrieved by the mis-selling of junk CCI, GAP and extended warranties typically added onto the purchase of a car, loan, credit card or

²² ASIC, Submission to FSRC, *Round 6: Insurance*, page 3: <https://financialservices.royalcommission.gov.au/Submissions/Documents/Round-6-written-submissions/POL.9006.0001.0192.pdf>; ASIC Report 492, A market that is failing consumers: The sale of add on insurance through car dealers.

home loan. Between 2016 and 24 September 2019, the tool has assisted people to make approximately 2,867 demands for refunds, totalling an estimated \$5.18 million.

An empirical analysis of letters of demand generated through the website reveals a damning picture of the mis-selling of CCI, GAP, and extended warranties. Remarkably, not a single user stated that would have decided to buy the add-on insurance knowing what they now know.

Of the 1,950 demands relating to CCI:

Consumer Credit Insurance	Yes	No	I don't know
If you had known what you know now, would you have decided to buy the insurance?	0%	100%	
Were your premiums added to your loan or credit card?	83%	8%	9%
Did you know you had bought the insurance?	61%	39%	
Did the salesperson tell you that you had to buy the insurance?	51%	49%	
Were you given an opportunity to go through the documents before agreeing to buy the insurance?	20%	80%	
Do you think the salesperson explained all the important exclusions and limitations?	3%	97%	
Did the salesperson explain your 'cooling off' rights?	11%	88%	
Did the salesperson pressure you into buying the insurance?	52%	48%	
Did the salesperson use other unfair sales tactics?	37%	63%	
Did the salesperson give you information that was misleading?	45%	55%	
Did the salesperson recommend the insurance to you personally based on something he or she knew about you, such as your age, state of health or employment status?	16%	33%	52%
Did you receive a product disclosure statement (PDS)?	46%	53%	
Overall, do you think the sales process was fair?	12%	88%	

Of the 790 demands relating to GAP insurance:

Guaranteed Asset Protection (GAP) Insurance	Yes	No	I don't know
If you had known what you know now, would you have decided to buy the insurance?	0%	100%	
Were your premiums added to your loan or credit card?	92%	8%	
Is there any reason why the policy was NOT suitable to you?	70%	5%	25%
Did you know you had bought the insurance?	68%	32%	
Did the salesperson tell you that you had to buy the insurance?	59%	41%	
Were you given an opportunity to go through the documents before agreeing to the purchase?	34%	66%	
Do you think the salesperson explained all the important exclusions and limitations?	6%	94%	
Did the salesperson explain the full cost of the insurance?	29%	71%	
Did the salesperson explain your 'cooling off' rights?	16%	84%	
Did the salesperson pressure you into buying the insurance?	64%	36%	

Did the salesperson use other unfair sales tactics?	51%	49%	
Did the salesperson give you information that was misleading?	56%	44%	
Did you receive a product disclosure statement (PDS)?	53%	47%	
Overall, do you think the process was fair?	10%	90%	

Of the 582 demands relating to extended warranties:

Extended warranties	Yes	No	I don't know
If you had known what you know now, would you have decided to buy the warranty?	0%	100%	0%
Was the cost of the warranty added to your loan or paid for by credit card?	72%	21%	8%
Did the salesperson explain the full cost of the warranty?	42%	58%	
Did you know you had bought the warranty?	86%	14%	
Did the salesperson tell you that you had to buy the warranty?	40%	60%	
Were you given an opportunity to review the documents before agreeing to the purchase?	34%	66%	
Do you think the salesperson explained all the important exclusions and limitations?	3%	97%	
Did the salesperson explain your 'cooling off' rights?	12%	88%	
Did you know the warranty was optional?	59%	41%	
Were you told (either in person, on the phone or in writing) that the salesperson would receive a commission for selling you this insurance?	3%	84%	13%
Did the salesperson pressure you into buying the warranty?	63%	37%	
Did the salesperson use any other unfair sales tactics?	44%	56%	
Did the salesperson suggest that the warranty would be the only protection you'd get if something went wrong with the car?	70%	30%	
Did the word 'warranty' make you think the product would work like a manufacturer's warranty?	86%	14%	
Did the salesperson give you information that was misleading?	63%	37%	
Did this information or lack of information influence your decision to buy the warranty?	84%	16%	
Did the salesperson recommend the warranty to you personally based on something he or she knew about you, such as your age, state of health or employment status?	24%	76%	
Did you receive a product disclosure statement (PDS)?	48%	52%	
Overall, do you think the sales process was fair?	15%	85%	

Impact on Victorian Aboriginal²³ communities

The Victorian Aboriginal Legal Service (**VALS**) and Consumer Action are currently running an integrated practice project to address some of the unmet consumer, credit and debt legal needs in Victorian Aboriginal communities.

²³ When we refer to Aboriginal communities, we include all Aboriginal and/or Torres Strait Islander peoples living within those communities. Consumer Action is located on the land of the Kulin Nations. We acknowledge all Traditional Owners of Country throughout Australia and recognise the continuing connection to lands, waters and communities. We pay our respect to cultures; and to Elders past, present and emerging.

The Project, which commenced around March 2019, involves work of various forms including regular community outreach and engagement sessions across Victoria.

The work of the IP Project suggests that the sale of unsuitable or junk add-on insurance is significantly impacting Victorian Aboriginal communities. Preliminary analysis of the legal enquiries being made through the community engagement sessions, conducted as part of the integrated practice project, indicates that add-on insurance or junk car warranties represents the third most common legal issue enquired about. All of these enquiries involve insurance added on to the purchase of a used car, while one of the cases involved the sale of a junk warranty (as opposed to CCI or GAP insurance). In many of these cases, the person has not specifically sought assistance of VALS or Consumer Action about the add-on insurance product but, rather, has sought assistance about unaffordable loans or the sale of poor-quality used cars. It is through the legal advice process, that these clients have found out that, unbeknownst to them, they have also been sold add-on car insurance along with their used car and/or unaffordable loan.

For stories of the rip-offs caused by this mis-selling, see Allan's story and Joe's story in Consumer Action's recent submission to ASIC's consultation on responsible lending.²⁴

Particular issues for mechanical breakdown insurance and warranties

Some warranties offer such a low level of cover that they are almost completely worthless to consumers. We share ASIC's view that there are particular issues with an effective intervention for mechanical breakdown insurance and warranties where the new or used car is still covered by a manufacturer's warranty.²⁵ Consumers lose money by paying a premium when cover will not start for 3 to 7 years, and in some cases will not be able to claim at all.²⁶ Given this, a deferred sales period (even with a 30-day deferral period) would be insufficient to stop the harm.

The extent of consumer harm in this area, including payment of premiums and interest for a useless product, requires a strong response. An appropriate intervention is to ban the sale of these products until 30 days prior to the expiration of any manufacturer's warranty, among other reforms.

We are also concerned about warranty providers selling 'dealer warranties' in an attempt to avoid the licensing and conduct obligations under the *Corporations Act*, the deferred sales process and external dispute resolution.²⁷ These products cause the same harm as warranty insurance and third-party warranties. Indeed, a number of the providers that previously structured their warranty offering as a regulated product have shifted to become 'dealer-issued' in recent years, while the underlying offer and branding remains the same. This appears to be a blatant attempt to avoid regulatory oversight.

We would support any steps to clarify whether or not these products fall within the *Corporations Act* exemptions. We consider that there are some 'dealer warranties' on the market that should not fall within the exemptions. We also consider that it is vital that this space is monitored closely to ensure avoidance does not ensue. It should be put beyond doubt that these products fall within ASIC's remit and the standard consumer protections applying to regulated warranties.

²⁴ Consumer Action Law Centre, Submission to ASIC, *Response to CP 309: Update to RG 209: Credit licensing: Responsible lending conduct*, May 2019, Case Study 4 (Allan's story), page 25 and Case Study 6 (Joe's story), page 36: <https://consumeraction.org.au/wp-content/uploads/2019/05/190520-Consumer-Action-Submission-ASIC-RG-209-Final.pdf>.

²⁵ As noted in ASIC CP 294, above n 14, para 239.

²⁶ ASIC CP 294, para 238.

²⁷ ASIC CP 294, paras 74-80.

Tim's story

Tim went to a used car dealership to upgrade his car. He traded in his old car and bought a newer model, which was financed by a loan arranged by the car dealership. The dealer also sold Tim a three-year used car extended warranty and roadside assistance. Tim knew from the dealer that the car would have a warranty but he did not know it would cost anything extra. Tim did not read the documents when he signed them, and the costs were not explained to him at the time. Tim is now paying back a high interest loan that covers the costs of the warranty and roadside assistance as well as the cost of the car. Tim's car has broken down multiple times since he bought it, and he has been unable to claim repairs on the warranty. When Tim called the dealership to ask for their help, the dealership informed Tim that the warranty did not cover those kinds of repairs, and that he had not met the warranty's servicing and mileage requirements, so he could not make a warranty claim.

Case study provided by Consumer Credit Legal Service WA

Extended warranties sold by retailers outside of the car yard also constitute a systemic exploitation. Extended warranties are analogous to junk insurance policies, as they offer very little (if any) real value, are sold at the same stage of the selling process and play on the same vulnerabilities and fears. Consumers are made to feel that they should purchase the product, as it is better to be "safe than sorry". This is a deceptive sales pitch, however, as consumers are already protected by the consumer guarantee provisions of the Australian Consumer Law—a fact which they are not always made aware of when purchasing the good.²⁸ While there has been legal action taken by consumer affairs regulators in relation to these forms of warranties, the outcomes have not resolved the consumer harm but have instead revealed deficiencies in the general law.²⁹

RECOMMENDATION 6. At a minimum, the following products should be subject to a Product Intervention Order (Tier One):

- a) Consumer credit insurance
- b) Guaranteed asset protection insurance
- c) Loan termination insurance
- d) Tyre and rim insurance
- e) Mechanical breakdown insurance and extended warranties, including "dealer-issued" warranties.

RECOMMENDATION 7. The sale and distribution of mechanical breakdown insurance and warranties should be regulated under a model that prohibits the sale of these products more than one month before the expiry of the manufacturer's warranty.

RECOMMENDATION 8. ASIC should seek clarity in relation to whether or not dealer warranties fall within the Corporations Act exemptions.

²⁸ For more information, see Consumer Action Law Centre, Submission to Consumer Affairs Australia New Zealand, *Australian Consumer Law Review*, 30 May 2016, pages 28-9: <https://consumeraction.org.au/wp-content/uploads/2016/05/Consumer-Action-ACL-Review-Submission-FINAL.pdf>.

²⁹ *Australian Competition & Consumer Commission v LG Electronics Australia Pty Ltd* [2018] FCAFC 96; *Director of Consumer Affairs Victoria v The Good Guys Discount Warehouses (Australia) Pty Ltd* [2016] FCA 22.

Tier 3: Case-by-case exemptions for products that meet relevant criteria

While in principle we do not support the exemption of any add-on insurance from a deferred sales model, we accept the recommendation of Commissioner Hayne that comprehensive car insurance should be excluded, subject to our Recommendations 2 to 4 above on additional criteria and conditions on exemptions.

RECOMMENDATION 9. Subject to Recommendations 2 to 4, comprehensive car insurance policies should be eligible to apply to ASIC for an exemption from the deferred sales model (Tier Three).

Tier 2: Products that should be subject to a deferred sales model

The deferred sales model should apply to all other add-on insurance products not identified above. In some cases, further investigation by ASIC may reveal that additional product belong in Tier One. Below we comment on particular types of add-on insurance.

Travel insurance

The deferred sales model should apply to add-on travel insurance. It is critical that travellers get an insurance policy that is suitable for their needs – too often people face shocking outcomes when a claim is denied due to an exclusion.³⁰ A deferred sales model will give people time to consider their insurance needs, and the conditions, benefits and exclusions under a particular travel insurance policy, away from pressure sales dynamics.

We would disagree with any argument that a Tier Three exemption is needed due to an imminent flight, and because coverage is provided immediately upon purchase. As the Productivity Commission noted,³¹ only 20% of people purchase travel insurance in the week prior to their departure.³² Most travel insurance is arranged 88 days before departure and 22 days after booking flights.³³

The risk of underinsurance is very low because there are other distribution channels than travel agents for buying travel insurance. Market research found that a 'wide range of methods are used to arrange travel insurance' with 31% buying direct from the insurer.³⁴ Anyone who wants or needs travel insurance can get it immediately through other channels, and likely for a better price. As discussed above and in the Proposals Paper, add-on travel insurance can be far worse value for consumers than stand-alone policies. Mystery shopping by price comparison revealed a dollar discrepancy of up to 205 per cent between insurance bought through an airline or holiday booking site compared with an online travel insurance specialist.³⁵ To the extent that travel insurance requires an exemption this should only be to allow the sale of add-on insurance where the travel is *commencing within the deferral period*. We note that the Productivity Commission did not suggest full exemption for add-on travel insurance but rather that the deferral mechanism may need to 'allow consumers purchasing flights shortly prior to departure to be able to buy add-on travel insurance if they genuinely desired it.'³⁶

³⁰ Clancy Yeates, 'Travel insurers to face ASIC scrutiny', The Age, 11 March 2019: <https://www.smh.com.au/business/banking-and-finance/travel-insurers-to-face-asic-scrutiny-20190310-p5131x.html>.

³¹ Productivity Commission, Competition Report, above n 8, page 430, footnote 116.

³² Nicole Pedersen-McKinnon, 'Families worst hit by Christmas travel insurance mark-ups', The Sydney Morning Herald, 20 November 2017: <https://www.smh.com.au/money/planning-and-budgeting/families-worst-hit-by-christmas-travel-insurance-markups-20171120-gzoqw6.html>.

³³ Quantum Market Research, *Survey of Australians' Travel Insurance Behaviour*, Prepared for the Insurance Council of Australia and the Department of Foreign Affairs and Trade, August 2016, page 27: <https://smartraveller.gov.au/guide/all-travellers/insurance/Documents/survey-travel-insurance-behaviour-web.pdf>.

³⁴ Ibid, page 22.

³⁵ Pedersen-McKinnon, above n 33.

³⁶ Productivity Commission, above n 8, page 430.

Ticket cancellation insurance

The deferred sales model should apply to ticket cancellation insurance. Further investigation by ASIC may require use of the PIP, given its low value. For example, we have seen one example of ticket cancellation insurance that cost \$14 to cover \$90 tickets. The policy provides cover if you crash on the way to the event, but only if the following onerous requirements are met: immediate medical attention was required; it didn't relate to an existing condition; proof of collision from an 'official body' is provided; and a doctor certified the claimant as unfit to attend the event.³⁷

Phone handset accidental damage insurance

The major carriers and some major electronics retailers offer insurance over mobile phone devices that is often sold as an add-on when a consumer purchases a mobile phone. Preliminary research by Australian Communications Consumer Action Network (**ACCAN**) indicates this insurance may be poor value, as it may duplicate cover in a consumer's home and contents or travel insurance and contain high premiums and excess payments relative to the amount of cover offered.³⁸ ACCAN's research also found that a number of the terms within these insurance contracts may be considered unfair.

The case study on repairs versus insurance costs in ACCAN's 2016 submission to the Australian Consumer Law Review demonstrates this problem:

Apple currently charges \$188.95 to fix a broken iPhone 6 screen.³⁹ The excess for a similar repair on the three insurance policies compared ranges from \$50 to \$125. Vodafone at \$125 with a \$15/month premium would require a consumer to make a claim every 4 months to 'break even'. The Optus breakeven point is slightly better at 10 months and JB HiFi's is at 8 months. Each of these policies requires a high number of claim events to break even on the combined costs of the premium and excess. Vodafone limits the policy to three claim events per 12 months. This means a consumer can never move beyond the breakeven point and would be equally well off without insurance.⁴⁰

The dynamics at the phone retailer are similar to observed problems with other forms of add-on insurance. As ACCAN states:

At the time of purchase, consumers are usually focussed on the features of the device rather than any add-on. As such, it is unlikely they will have the ability to adequately weigh up the premium, excess and likelihood of making a claim. In this context, combined with the exclusions outlined above, consumers are left with a contract of such poor value that it could in its entirety be considered unfair.⁴¹

As with other areas of financial services, products in the telecommunications industry can be designed to avoid consumer protections. We note the emergence of insurance-like add-on products that promise to repair or replace phone handsets that providers don't classify as insurance, meaning no insurance-related protections apply. For example, Telstra states that its StayConnected product,⁴² the new iteration of its previous device replacement scheme offered at point of sale, is not insurance because it does not require an 'event' and it includes data backup.⁴³

³⁷ CoverMore, Ticketek Ticket Insurance, *Combined Financial Services Guide and Product Disclosure Statement* (effective 1 June 2017): https://premier.ticketek.com.au/content/pdf/Ticket_Insurance/ProductDisclosureStatement.pdf.

³⁸ ACCAN, Submission to Consumer Affairs Australia New Zealand, *Australian Consumer Law Review 2016*, May 2016, page 18: <https://accan.org.au/files/Submissions/Australian%20Consumer%20Law%20Review%20ACCAN%20submission.pdf>.

³⁹ Ibid, page 10, citing Apple, 2016, 'iPhone screen repair costs', available at: <https://support.apple.com/en-au/iphone/repair/screen-damage>

⁴⁰ Ibid, page 10.

⁴¹ Ibid, page 10.

⁴² See: <https://www.telstra.com.au/support/category/mobiles-tablets/plans/stayconnected-plus>.

⁴³ See: <https://crowdsupport.telstra.com.au/t5/Mobiles-Tablets/Stay-Connected-FAQ-s/ta-p/386601>.

It can also only be added at the time of purchase (not later) which will result in pressure sales, there is no cooling off period, and it requires a monthly fee of \$15/month as well as a replacement or screen fix fee when used.⁴⁴ These products should be subject to further investigation and potential regulatory action.

RECOMMENDATION 10. All other insurance products sold as an add-on to a primary product or service should be sold via a deferred sales model (Tier Two).

Request for Feedback 2: Please provide feedback on how this trigger would correspond to your current business practices in selling add-on insurance products

Trigger event

The Proposals Paper recommends that the deferral period be triggered by the following steps taking place in the specified order:

- Step One: The consumer makes a 'financial commitment' to purchase the good/service and/or arranges finance.
- Step Two: The retailer provides prescribed information about the add-on insurance product which includes details about the deferral period following the financial commitment to purchase of primary product. A financial commitment may involve paying a deposit or making an application for finance.

Step One: 'Financial commitment'

We recommend that the deferral period only begin once the primary good or service has been purchased, financed *and* delivered to the consumer, and the prescribed information has been provided.

We are strongly opposed to the proposal that the deferral period is triggered by the consumer merely making a 'financial commitment' such as paying a deposit or applying for finance. This proposal would mean that, in many cases, the consumer will need to re-engage with the salesperson to take possession of the good or sign the loan contract, which means they are at risk of add-on insurances being bundled into the loan.

This proposal allows a retailer to sell add-on products before the consumer has taken delivery. The well-documented problems in mixing the two sales processes including confusion and other behavioural biases are still at play. A deferred sales model that allows pressure sales will defeat the very purpose of the reform.

Principles for an effective trigger

The following principles should inform the trigger event under an effective deferred sales model:

1. *The good/service should be purchased before the add-on insurance sale:* As ASIC found in the car yard context, if add-on products are offered before the purchase, a consumer cannot make an informed decision about the add-ons, and is more likely to experience decision fatigue.⁴⁵
2. *Finance should be approved before the add-on insurance sale:* Similarly, the finance process must be clearly separated from the add-on sales process. Consumers must not be led to believe that purchasing add-on insurance will improve their chances of finance approval or the terms on which finance is offered. While this may lead to an additional financing approval process being required, if the add-on insurance is

⁴⁴ See: <https://www.telstra.com.au/mobile-phones/mobiles-on-a-plan/stayconnected>.

⁴⁵ ASIC, CP 294, above n 14, Figure 1, Sales sequence C, page 52.

ultimately financed, this is an important financial decision for both the financier and the purchaser to consider separately. This provides a significant opportunity to inform and engage the mind of the consumer on the consequences of the decision to purchase an add-on insurance product on finance. Our services have seen car finance contracts where the add-on products are equal or greater in value to the cost of the car – this is a substantial purchase with significant financial implications, particularly when attracting interest, which in some cases is very high (e.g. 48% per annum).

3. *The good should be delivered before the add-on insurance sale:* Consumers need to be in possession of the good before true consideration of the distinct add-on products can be undertaken. This model wholly removes the add-on insurance sales process from the point of sale and the high-pressure techniques that being on the salesperson territory can entail. A consumer would no longer have to worry about having to please a salesperson in order to ensure a smooth transition to final possession of the good or service.
4. *The decision to purchase and finance a good must be distinct from the decision to purchase and/or finance an add-on insurance product:* The central aim of the model should be to ensure that the decision to purchase a vehicle and the decision to purchase an insurance product are clear and distinct. The deferral period and its commencement must be designed to promote this as much as possible. This model separates the purchase decisions completely and removes any inference (express or implied) that the purchase of the add-on products can influence final approval of the finance or any other aspect of the sale.
5. *The customer should know the total cost of add-on insurance before the deferral period starts:* The deferral period should not commence until the car dealer gives the consumer the complete cost of add-on products for their specific vehicle and finance arrangements.

Our recommendation that the deferral period start after purchase, delivery, and any finance approval meets these principles. It will provide simplicity, certainty for distributors and for supervisors, improved clarity of decision-making and allow consumers the space to consider their needs for add-on insurances.

RECOMMENDATION 11. The deferral period should only begin once the primary good or service has been purchased, financed *and* delivered to the consumer, and the prescribed information has been provided.

Step 2: Retailer provides prescribed information

We support this proposed requirement. Consumers should have useful product information regarding an add-on insurance product and engage with it before the deferral period starts. This will enable the consumer to make a genuinely informed assessment.

The current disclosure requirements for add-ons sales have not ensured that people understand what they are buying.⁴⁶ It is now widely accepted that traditional disclosure models, chiefly the Product Disclosure Statement (PDS), are similarly ineffective.⁴⁷ Even when a person is buying insurance as a primary purchase, they are highly unlikely to read the PDS. Research commissioned by the Insurance Council found that 81 per cent of people did not read the PDS before buying their comprehensive car insurance.⁴⁸

Our casework has shown that the vast majority of people do not understand the add-on products they have bought. Concerningly, 39 per cent of DemandARefund.com users did not even know they had bought consumer credit

⁴⁶ ASIC, CP 294, above n 14, paras 111-117.

⁴⁷ Financial System Inquiry, *Final Report*, November 2014, page 193; ASIC, Submission to FSRC, *Round 6: Insurance*, pages 7-11.

⁴⁸ Insurance Council of Australia, *Consumer Research on General Insurance Product Disclosures: Research findings report*, February 2017, page 18.

insurance. Due to the low-value and high cost of many add-on products, we believe that a significant number of people who buy add-on products would not have done so if they understood what they were being sold.

We support the proposal that ASIC determine the format, content, and mode of delivery of the prescribed information.

We also support the list of potential inclusions in the prescribed communications listed at page 13 of the Proposals Paper, in particular the inclusion of claims ratios.

The prescribed information should also make it clear that the add-on products may be available at competitive prices elsewhere, *including directly from the insurer/warranty company*. ASIC has reported on the high cost of add-on products in car yards compared with the same products bought directly from the insurer—pointing to a factor of up to ten times.⁴⁹ Insurers must also ensure that the consumer understands the total cost of the add-on products, including interest and fees (and the total cost including interest if the premium is to be financed). As the Proposal Paper notes, CHOICE found add-on travel insurance policies that were more than twice the cost of buying a standalone policy from the same underwriter.⁵⁰

Treasury should consider the consequences for a retailer that provides information about the add-on product before the financial commitment is made. Will this be specifically prohibited? Will it be a breach of the law and what would be the penalty and consumer remedy? How would this be prevented? How would it be documented?

We recommend that the communication approach should be consumer tested before it is rolled out and refined over time.

The consumer communication requirements that should apply under a deferred sales model were considered in detail in ASIC Consultation Paper 294.⁵¹ For further information and recommendations on the form, content and delivery of consumer communications, see the Joint Consumer submission to ASIC CP 294 at pages 13-19, which is included for Treasury's reference at **Appendix B**.

RECOMMENDATION 12. Innovative, interactive consumer communication techniques should be mandated and supervised to ensure greater consumer understanding and purchase of suitable add-on insurance products. To ensure this, we support a standardised model that is active/interactive and not passive (that is simply providing a piece of paper); and includes a series of 'filter' or 'knock out' questions, before the purchase of the product.

Duration of deferral period

We strongly recommend that the deferred period be extended from four days to a minimum of seven days, consistent with the recommendation of the Productivity Commission. This would reduce the risks of pressure selling and give consumers an opportunity to understand the add-ons offered by dealers.

The longer the period, the more distinct and disruptive the processes will be and therefore the greater the potential benefit to consumer decision-making. There is considerable merit in introducing a 30-day deferral period for some products to allow a consumer to fully assess their financial situation before purchasing add-on insurance. A

⁴⁹ ASIC, Report 471, *The sale of life insurance through car dealers: Taking consumers for a ride*, 29 February 2016, para 80: <https://download.asic.gov.au/media/3549384/rep471-published-29-february-2016.pdf>.

⁵⁰ <https://www.choice.com.au/travel/money/travel-insurance/articles/flight-travel-insurance>; Proposals Paper page 5.

⁵¹ Above n 14.

consumer would have made at least one payment towards any financing, allowing the consumer to better assess their financial situation and their ability to finance extra insurance.

The Productivity Commission considered that, in principle, a deferred sales model could enhance consumers ability to impose competitive pressure on insurers and product retailers by allowing consumers to consider the merits and appropriateness of the add-on product and to shop around for alternatives. It observed that:

In practice, this hinges on the model giving a sufficiently long break between the purchase of the primary product and the point at which the consumer can purchase the add-on product to allow the 'halo effect' to dissipate and the consumer to be able to dispassionately assess their need for insurance and consider the products available to them.

The four-day deferral period of the Banking Code of Practice deferred sales model is insufficient to achieve this end. As the deferral period commences at the point at which the credit card application is submitted, the model can potentially allow CCI to be sold prior to credit approval.

The Commission's view is that the deferral period should be a minimum of seven days from the point at which the consumer applies for the credit product.⁵²

The Proposals Paper does not state why the Productivity Commission's recommendation of a 7-day deferral has not been adopted.

However, the length of the deferral period should not be the primary mechanism for separating the sale of the primary product and uptake of finance from the sale of add-on products. The deferred sales model would likely fail if it relied on the number of days in a transaction having this effect. For example, if a four-day (or even seven-day) deferral period meant that a car dealer could simply ask the customer to pick up the car on Thursday rather than Tuesday, and could sell add-on products before the car purchase and finance are finalised, the deferral period may have no benefit.

The central mechanism to ensure distinct sales processes and purchasing decisions is in our view, the commencement of the deferral period being upon delivery following purchase, approval of any finance and delivery of any goods.

RECOMMENDATION 13. Extend the deferral period to a minimum of seven days from the trigger event.

Initiating contact

A more effective model would require that only the consumer, not the retailer, could initiate contact to accept (or decline) the add-on insurance at the end of the deferral period.

However, as a compromise, we accept the Government's proposal that the retailer could only contact the consumer once via written correspondence at the end of the deferral period. The method of written contact should be by the consumer's choice of email, text or hard copy mail.

We support the position that telephone contact by the retailer to the consumer will not be permitted at the end of the deferral period. There is overwhelming evidence of the harm caused by high pressure phone sales, including through the Financial Services Royal Commission and ASIC's work into outbound sales of life and consumer credit

⁵² Productivity Commission, Competition Report, above n 8, page 29 (internal citations omitted).

insurance. Telephone contact at the end of the deferral period should be prohibited to prevent the issues arising from direct selling of life insurance and CCI shifting to other forms of add-on insurance.

Customer initiated completion of sale

We are strongly opposed to the proposal to allow consumers to opt-in to the purchase of the add-on insurance after one day.

This proposal is at serious risk of abuse and regulatory arbitrage. It is inconsistent with Royal Commission Recommendation 7.3 that exceptions and loopholes be minimised. There is nothing in the model to stop a sales representative from telling the consumer that to secure finance or a 'discounted' price, they must contact the retailer the next day to complete the purchase. This is particularly risky when combined with the current proposed trigger event of an application for finance, because consumers may feel pressured to follow the salesperson's suggestion in order to secure finance.

In effect, the one-day customer-initiated completion of sale will convert the deferral period from four days to one day, which is wholly inadequate to prevent the ongoing harm.

If a person wants to immediately obtain an insurance product that suits their needs – they can. Many add-on insurances are sold by other distributors or by the insurer directly and are usually much cheaper. For those add-on products that are only sold through the retailer distribution channel, the deferred sales model should encourage competition from new entrants. In the car yard context, ASIC observed that:

Because consumers would have a greater opportunity to obtain information about other competing products, providers currently locked out of car dealership distribution points could be encouraged to offer add-on products online. If online distribution becomes widespread, it could generate increased competition between providers and improve transparency on product price and cover, benefitting all parties.⁵³

We note that this proposal is industry-friendly and would actually give sellers a benefit. Currently, there is a cooling-off period for add-on insurance, usually around 30 days.⁵⁴ If the deferral period – currently proposed to be 4 days – is less than the cooling-off period, then sellers are still getting a benefit from this reform. That is, if the consumer opts in after the deferral period, the seller knows they have a completed sale; at present, they don't really know they have a sale until the end of the cooling-off period.

We support the option for the consumer to reject the sale entirely during the deferral period. Those who read the prescribed period and decide that the product is not for them should be able to communicate this without receiving further communications at the end of the deferral period.

RECOMMENDATION 14. Remove the customer-initiated completion of sale from the deferred sales model for add-on insurance.

Enforcement and commencement

Monitoring

We support the Government giving ASIC responsibility for monitoring and enforcing the regime to ensure distributors are complying with the deferred sales model. This will require ASIC to undertake significant data

⁵³ ASIC, CP 294, above n 14, para 187.

⁵⁴ <https://www.moneysmart.gov.au/insurance/car-insurance/add-on-insurance>.

collection and, as discussed above, investigation as well as specific monitoring programs. The Government should ensure ASIC has adequate resourcing to effectively monitor and enforce the regime.

We note that ASIC proposed enhanced supervision obligations for car dealers in Consultation Paper 294. There is overwhelming evidence that insurers' current supervision of the car dealer channel for add-on insurance sales is 'manifestly inadequate'.⁵⁵ While insurers have acknowledged that the commissions they pay to car dealers lead to unfair and misleading sales, we agree that addressing commissions alone will not necessarily see benefits flow to consumers.⁵⁶

The problems with add-on insurance and warranties often materialise when people make a claim. While insurers profit from add-on insurance mis-selling, they also bear the burden of it through claims disputes and regulatory intervention. Improved supervision is in the interests of both consumers and industry.

We supported ASIC's proposal of the use of risk indicators to allow early intervention where a particular dealership is selling add-on products in a way that is non-compliant or unfair.⁵⁷

Other measures which would improve supervision and compliance include:

- Analysis of the data collected through filter and knock out questions (discussed above) to check whether dealers are selling policies to people for whom they are unsuitable.
- Benchmarking and analysis of claims experience data (discussed above), including denied claims, which may indicate a higher level of unsuitable sales in some dealerships. We would expect this data to improve over time.
- Benchmarking and analysis of penetration rates. We would also expect penetration rates to improve over time.

Penalties

We strongly support the introduction of criminal civil and administrative penalties for breaches of the deferred sales model. The history of rampant mis-selling of low value add-on insurance evidences the need for effective deterrence and swift action for breaches.

Consumer remedies

The final model should include adequate remedies for affected consumers in the event of a breach of the deferred sales model. As a matter of principle, the remedies should be sufficient to put the consumer back in the position they would have been, but for the breach, and to deter breaches in the first place. As an absolute minimum, this would mean the consumer should be able to void the policy, obtain a refund of premiums paid and any consequential damage flowing, such as interest paid on financed premiums.

Even with the success of DemandaRefund.com, multiple ASIC remediation schemes, and class actions underway, it is likely there are consumers who have been mis-sold add-on insurance that have not yet been compensated because they do not even know they have it.

Given the difficulties, delay and expense involved in cleaning up the mess afterwards – estimated to be up to \$1 billion – it is essential that the consequences for breaching the deferred sales model are sufficient to deter

⁵⁵ ASIC, CP 294, above n 14, para 247.

⁵⁶ ASIC, CP 294, above n 14, paras 250, 253.

misconduct in the first place. Insurers should establish systems which will not only prevent and detect mis-selling but provide quick and complete remediation to victims of mis-selling. Remediation schemes should be designed at the same time as monitoring and compliance systems.

Commencement

To minimise the ongoing consumer harm, the period of time between passage of the legislation and commencement of the deferred sales model should be a maximum of 12 months, and ideally six months or less.

RECOMMENDATION 15. The final model should include consumer remedies for breach of the deferred sales model. Remedies should be sufficient to put the consumer back in the position they would have been and to deter breaches.

RECOMMENDATION 16. Remediation schemes should be designed at the same time as monitoring and compliance systems.

RECOMMENDATION 17. The commencement of the deferred sales model should be a maximum of 12 months, and ideally 6 months or less, from passage of the legislation.

Other implementation issues

Bridging insurance

We strongly agree with ASIC that the risk of being uninsured during the deferral period is very small and this period does not create a need for 'bridging' cover,⁵⁸ which is neither practical nor desirable.

The legislation should ensure that there is no ability to undertake regulatory arbitrage with the creation of bridging insurance. Insurers should not be able to offer 'bridging' cover during any deferral period. This would not address the small risk involved in the lack of coverage during the deferral period, and could perpetuate high-pressure selling and distort consumer decision-making.

We note that comprehensive car insurance (which covers a very real and present risk) is not included in this model and will still be available before the consumer takes the delivery of the vehicle or drives it.

Many add-on insurance policies and warranties currently include waiting periods, during which the customer is not covered.

It is difficult to understand any industry concern that consumers will not be covered from the moment they drive away from the car yard when this has been the status quo for a significant time. If insurers were genuine in their concern and wish to reduce the time in which people are not covered by an add-on product, they should remove the waiting periods from existing add-on and other insurance products.

'Bridging' insurance would establish a new opportunity for high-pressure selling in car yards. It would also have the 'endowment effect' or exploit the consumers' 'status quo bias',⁵⁹ by making them feel invested in the bridging product, and, because they have something akin to the add-on product, that the add-on product has some intrinsic value. This would distort people's decision-making and make them more inclined to buy add-on products after the deferral period. If car dealers used incentives or discounts to buy add-on insurance, the risk of poor decision-making would significantly increase.

⁵⁸ ASIC, CP 294, above n 14, para 212.

⁵⁹ See Daniel Kahneman, Jack L. Knetsch, Richard H. Thaler, Anomalies: The Endowment Effect, Loss Aversion, and Status Quo Bias, *The Journal of Economic Perspectives* 5(1), pp 193-206, Winter 1991.

RECOMMENDATION 18. The legislation should ensure that there is no ability to undertake regulatory arbitrage with the creation of 'bridging' insurance during the deferral period.

RECOMMENDATION 19. Insurers should reduce or remove waiting periods altogether in add-on products to reduce the period in which consumer are uninsured.

Interaction with ban on unsolicited selling of insurance

It is clear that many people have been sold add-on insurance that they did not intend to buy – thus falling within a common understanding of what is unsolicited. Treasury should consider the interaction of these reforms to add-on insurance with:

- the forthcoming ban on unsolicited selling of insurance (FSRC Recommendation 4.1);
- Commissioner Hayne's statement that it is 'desirable' to introduce a statutory definition of what is 'unsolicited';⁶⁰ and
- ASIC's regulatory guidance on the anti-hawking provisions.⁶¹

Contact details

Please contact Senior Policy Officer **Cat Newton** at **Consumer Action Law Centre** on 03 9670 5088 or at cat@consumeraction.org.au if you have any questions about this submission.

Yours Sincerely,

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⁶⁰ FSRC, *Final Report: Volume 1*, above n 4, page 283.

⁶¹ ASIC, *Regulatory Guide 38: The hawking provisions*, 1 May 2005.

Appendix A: About the Contributors

Consumer Action Law Centre

Consumer Action is an independent, not-for profit consumer organisation with deep expertise in consumer and consumer credit laws, policy and direct knowledge of people's experience of modern markets. We work for a just marketplace, where people have power and business plays fair. We make life easier for people experiencing vulnerability and disadvantage in Australia, through financial counselling, legal advice, legal representation, policy work and campaigns. Based in Melbourne, our direct services assist Victorians and our advocacy supports a just marketplace for all Australians.

Consumer Credit Legal Service (WA) Inc

Consumer Credit Legal Service (WA) is a not-for-profit charitable organisation which provides legal advice and representation to consumers in WA in the areas of banking and finance, and consumer law. We strengthen the consumer voice in WA by advocating for, and educating people about, consumer and financial, rights and responsibilities. In the 2018/2019 financial year, we represented over 100 clients in their disputes, and participated in over 40 law reform activities.

Financial Rights Legal Centre

The Financial Rights Legal Centre is a community legal centre that specialises in helping consumers understand and enforce their financial rights, especially low income and otherwise marginalised or vulnerable consumers. We provide free and independent financial counselling, legal advice and representation to individuals about a broad range of financial issues. Financial Rights operates the National Debt Helpline, which helps NSW consumers experiencing financial difficulties. We also operate the Insurance Law Service which provides advice nationally to consumers about insurance claims and debts to insurance companies, and the Mob Strong Debt Help services which assist Aboriginal and Torres Strait Islander Peoples with credit, debt and insurance matters. Financial Rights took close to 25,000 calls for advice or assistance during the 2017/2018 financial year.

Appendix B: Joint submission to ASIC Consultation Paper 294

Available at: <https://consumeraction.org.au/joint-submission-options-to-reform-the-sale-of-add-on-insurance-and-warranties-in-car-yards-2/>.