Law Council
OF AUSTRALIA

Legal Practice Section

25 October 2017

Australian Securities and Investment Commission
GPO Box 9827
CANBERRA ACT 2600

By email: add-on.consultation@asic.gov.au

Dear Sir/Madam

Submission on Consultation Paper 294: The sale of add-on insurance and warranties through caryard intermediaries

1. This submission has been prepared by the Australian Consumer Law and National Insurance Lawyers Committees of the Law Council's Legal Practice Section (**the Committees**).[1] The Committees welcome the opportunity to provide comments to Australian Securities and Investment Commission (**ASIC**) on Consultation Paper 294: *The sale of add-on insurance and warranties through caryard intermediaries* (**Discussion Paper**).

2. The Committees strongly endorse the two proposals made by the Consultation Paper, being:

   - a deferred sales model which would insert a pause into the sales process for add-on insurance and warranties regulated by the *Corporations Act 2001* (Cth) other than comprehensive or compulsory third-party insurance products (**Proposal 1**); and

   - the introduction of more robust and targeted requirements for providers to meet when supervising and monitoring their authorised representatives (**Proposal 2**).

<u>Deferred sales model</u>

3. A deferred sales model addresses the central consumer harm identified in the previous reports published by ASIC in relation to add-on insurance, that is, the opportunity for pressure and unfair sales tactics involved in bundled selling of a motor vehicle with finance and add-on insurance.[2]

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1 The Law Council of Australia is a peak national representative body of the Australian legal profession. It represents the Australian legal profession on national and international issues, on federal law and the operation of federal courts and tribunals. The Law Council represents 60,000 Australian lawyers through state and territory bar associations and law societies, as well as Law Firms Australia.

2 See Australian Securities and Investment Commission, *Buying add-on insurance in car yards: Why it can be hard to say no*, Report No 470 (26 February 2016); Australian Securities and Investment Commission, *The sale of life insurance through car dealers: Taking consumers for a ride*, Report No 471 (29 February 2016); Australian Securities and Investment Commission, *A market that is failing consumers: The sale of add-on insurance through car dealers*, Report No 492 (12 September 2016).

4. While consumer harm is also caused by other factors, for example, the design of products that offer restricted or limited benefits, or financing the premium for add-on insurance, it is the sales channel itself which is a core reason why consumers are disadvantaged in relation to the purchase of add-on insurance. For this reason, the Committees strongly endorse Proposal 1. If enacted, it would provide consumers with additional time to navigate the complexities of add-on products and facilitate improved decision making.

Commencement period for the deferral period

5. The Consultation Paper seeks feedback about the commencement point for the deferral period. The Committees submit that any deferral period will be most effective if it begins when the vehicle has been purchased by the consumer and consumer communication has been provided. When compared to the ‘date of delivery option and consumer information provided’ commencement point option, the ‘time of purchase option’ has the advantage of:

   - Avoiding potentially significant delays between initial provision of consumer information (most likely to occur at time of purchase). For example, it is common for delivery of new cars to occur after a period of one month or more following the sale. Such delay would potentially increase consumer inconvenience and decrease consumer understanding as the initial provision of consumer information and explanations provided at point of sale are likely to have dimmed in the consumer’s recollection.

   - Avoiding an enforced period where the consumer is not insured. Contrary to the position in CP294, this could be significant. While the chance of an insured event occurring within the deferral period may be relatively low, the potential financial consequences for an individual consumer could be significant. The risk would be greater if combined with a relatively longer deferral period.

6. Moreover, the deferral period itself is sufficient to provide consumers with the opportunity to assess the benefits of the add-on insurance, research other sources of supply of similar add-on insurance or alternative insurance options.

7. The Committees acknowledge the concern expressed in the Consultation Paper that this option may create the opportunity for pressure that would arise if the conclusion of the deferral period could be aligned with the point of delivery of the vehicle. The Committee considers that this concern is outweighed by the above advantages of the time of purchase option and can the managed by the innovative consumer information approaches discussed below and the consumers’ access to independent sources of information and competing distribution sources and products.

8. This option would most clearly reflect ‘Sales Sequence B’ as outlined in the Consultation Paper. The paper notes disadvantages with this option including that the consumer and lender may need to adjust loan amounts or term to allow for additional costs. From a consumer perspective, this may in fact be an advantage as it will separate the decisions relating to the finance, that is, one decision about financing the purchase of the vehicle and a separate decision relating to extending that finance to cover the cost of add-on products. This would seem to support the policy justification of the deferred sales mechanism by unbundling the multiple purchases and facilitating better decision making.

Duration of the deferral period

9. The Committees submit that the fact of deferral is more important than the period of deferral. The Committees support a four-day deferral period because it would:

- Provide a sufficient deferral period to accrue the intended benefits of:

  - separating the purchase decision from the car and finance purchase decisions;

  - lessening the effect of any unfair sales practices; and

  - providing consumers with the opportunity to independently assess the benefits of the add-on insurance and research other sources of supply of similar add-on insurance or alternative insurance options.

- Minimise the risk of consumer inconvenience and decreased consumer understanding which may arise from a longer period between the initial provision of consumer information and explanations (provided at point of sale) and purchase decision due to the dimming of the consumer's recollection of such material.

- Align the deferral period with the Australian Banking Association's proposed four-day deferral period in relation to the sale of consumer credit insurance with credit cards purchased in branches or over the phone.[3] There may be benefits in aligning the deferral periods to enable community understanding about the legal requirements for sales practices involving these products.

Consumer communication

10. The Committees support the provision of specific information being provided to consumers before the beginning of the deferral period. This should not, however, be a mere information sheet. The limitations of paper-based disclosure are well-known, and consideration should be given to more innovative disclosure mechanisms.

11. The Committees endorse the Consultation Paper's comments in respect of online (or app based) communications including a degree of standardisation. Any guidelines should, however, provide sufficient flexibility to allow for product differentiation and competition between insurers.

12. Any online or app based approach could also require consumers to be asked specific questions through an online form which would 'knock them out' if they were ineligible for the product or if it provided limited benefit (eg the purchase involved such a substantial deposit that there would likely not be any "gap" in the case of guaranteed asset protection (GAP) insurance).

13. Consumers should be informed of the availability of independent sources of information and alternative distribution sources and products.

14. The Committees support measures to test consumer comprehension after the consumer buys the product by monitoring trends in consumer behaviour. At this stage, and subject to the results of the above trend analysis, comprehension tests prior to

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3 Australian Securities and Investment Commission, 'Banks to overhaul consumer credit insurance sales processes' (Media Release 17-255, 1 August 2017) <http://asic.gov.au/about-asic/media-centre/find-a-media-release/2017-releases/17-255mr-banks-to-overhaul-consumer-credit-insurance-sales-processes/>.

purchase are not supported as it introduces additional consumer inconvenience and may act as a barrier to purchase not necessarily aligned to the needs of the consumer.

Mechanical breakdown insurance and warranties

15. The Committees agree that there are significant consumer problems associated with the sale of mechanical breakdown insurance and third-party warranties where the vehicle is still covered by the manufacturer's warranty. The cover offered by these products might not kick in until many years after the purchase of the property and, in some instances, after the sale of the vehicle. The Committee supports a proposal whereby the sale of such products was not allowed until a date calculated by reference to the expiry of the manufacturer's warranty. We would suggest a period of 6 months prior to the expiry of the manufacturer's warranty. At such time, the consumer would be in a better position to assess the purchasing decision.

16. The Committees are aware that some add-on products have been designed to escape the coverage of the *Corporations Act*, for example, dealer-issued warranties that are administered by third parties. The Committee encourages ASIC to consider mechanisms by which this type of avoidance can be addressed.

Enhanced supervision obligations

17. The Committees endorse the proposal to require insurers and other providers of add-on products to have controls in place to prevent dealers and salespeople in caryards from engaging in unfair conduct at the point of sale. As stated by the Consultation Paper, the current level of supervision and monitoring by providers and their authorised representatives is inadequate.

18. Recognising that it is high commissions that can drive the conduct of dealers and salespeople, and the challenges for product issuers in monitoring sales in dispersed caryards, there is a clear case for improved standards for supervision. One option that might be adopted is for product issuers to be required to develop comprehensive oversight policies and practices, including the use of risk indicators and mystery shopping. Where problematic practices are identified, the product issuer should clawback commissions and ensure affected consumers are compensated.

Contact

19. The Committees would welcome the opportunity to discuss the submission further. Please contact John Farrell, Policy Lawyer, at john.farrell@lawcouncil.asn.au or (02) 6246 3714, if you would like further information or clarification.

Yours sincerely

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