

Mr John Hawkins
Committee Secretary
Senate Economics Legislation Committee
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4 August 2009

Dear Mr Hawkins

TRADE PRACTICES AMENDMENT (AUSTRALIAN CONSUMER LAW) BILL 2009

The Insurance Council of Australia Limited¹ (Insurance Council) refers to your letter of 7 July 2009, and appreciates the opportunity to comment on the Trade Practices Amendment (Australian Consumer Law) Bill 2009 (the Bill) which was referred to the Senate Economics Legislation Committee (the Committee) on 25 June 2009.

The Insurance Council strongly supports the establishment of a national regime of consumer protection. By eliminating inconsistencies between jurisdictions, a national regulatory regime will create greater certainty as to what is the law, thereby increasing the likelihood of better compliance. Compliance costs should also be lower as businesses with national reach (the majority of Insurance Council members) will not have to take account of variations in the law in different jurisdictions.

This submission addresses several aspects of the Bill of particular interest to general insurers.

Unfair Contract Terms

As explained in Insurance Council's submissions to Treasury of 27 March and 26 May 2009 responding respectively to the consultation paper on an Australian Consumer Law and draft provisions on unfair contract terms (copies enclosed), Australian retail consumers of general insurance already benefit from a strong, predominantly national, regulatory regime specifically through the Insurance Contracts Act 1984 (Insurance Contracts Act), and also through the Corporations Act 2001 (Corporations Act), and the ASIC Act 1999 (ASIC Act). The Insurance Contracts Act and the Corporations Act provide protection against unfair contract terms. Additionally, there are provisions in all three laws that guard against unfair or unconscionable conduct.

Section 15 of the Insurance Contracts Act excludes insurance contracts from the operation of a Commonwealth, State or Territory Act that provides relief in the form of judicial review of unfair contracts or the making of a misrepresentation except for relief in

¹ The Insurance Council of Australia is the representative body of the general insurance industry in Australia. Our members represent more than 90 percent of total premium income written by private sector general insurers. Insurance Council members, both insurers and reinsurers, are a significant part of the financial services system. March 2009 Australian Prudential Regulation Authority statistics show that the private sector insurance industry generates gross premium revenue of \$31.7 billion per annum and has total assets of \$93.8 billion. The industry employs approx 60,000 people and on average pays out about \$99.2 million in claims each working day.

Insurance Council members provide insurance products ranging from those usually purchased by individuals (such as home and contents insurance, travel insurance, motor vehicle insurance) to those purchased by small businesses and larger organisations (such as product and public liability insurance, professional indemnity insurance, commercial property, and directors and officers insurance).

the form of compensatory damages. This provision originated in the Australian Law Reform Commission's conclusion that in light of the utmost good faith obligation, it was unnecessary for insurance contracts to be subject to a facility for judicial review of unfair contractual terms.² The Panel which reviewed the Insurance Contracts Act several years ago concluded that the exclusion provided by section 15 was still valid.³

Consequently, in view of the strong protection already provided to insureds, the Insurance Council endorses as entirely appropriate that the Bill does not alter the exemption provided under section 15 of the Insurance Contracts Act. This is the basis upon which unfair contract term provisions have operated in Victoria⁴ without any consumer detriment being reported.

In addition to the exclusion for insurance contracts provided by section 15 of the Insurance Contract Act, operation of the unfair contract terms provisions will not apply to terms required or expressly permitted by a law of the Commonwealth or a State or Territory.⁵ This is important because several of the examples of potentially unfair contract terms contained in the Bill are specifically permitted by the Insurance Contracts Act.⁶

Prohibition of Indemnification of Monetary Penalties

The Bill introduces civil penalties into the Trade Practices and ASIC Acts for contraventions in relation to:

- unconscionable conduct;
- unfair practices;
- pyramid selling;
- product safety and information;
- use of prohibited terms; and
- failing to respond to a substantiation notice or providing false or misleading information in response to a substantiation notice.

The ASIC Act will be amended to include provisions (Section 12GBD) mirroring existing sections 77A, 77B and 77C of the Trade Practices Act (see Attachment A) prohibiting the indemnification of officers of bodies corporate in relation to the payment of pecuniary penalties. The Trade Practices Act provisions closely follow section 199A of the Corporations Act. (See Attachment B for relevant Corporations Act provisions.)

Division 1 of Part 2D.2 of the *Corporations Act* restricts the scope of company indemnities and company-funded Directors and Officers (D&O) insurance policies.⁷ As you will appreciate, the public policy goal behind these restrictions is to prevent companies from shielding directors and officers from liability, whether by way of indemnification or through the payment of D&O insurance premiums. Otherwise, companies could undermine the law by removing the force and effectiveness of provisions in the *Corporations Act* which impose responsibilities, and concomitant liabilities, on directors and officers.

² Australian Law Reform Commission 1982, Insurance Contracts ALRC 20, para 51.

³ Review of the Insurance Contract Act 1984, Final Report on second stage, page 53.

⁴ Information provided to Insurance Council by Commonwealth Treasury at a meeting on 13 May 2009.

⁵ The Australian Consumer Law: Consultation on draft provisions on unfair contract terms, page 17.

⁶ For example, "A term that permits or has the effect of permitting one party but not the other to avoid or limit the performance of the contract" and A term that permits or has the effect of permitting one party but not the other to terminate a contract.

⁷ D&O policies cover directors and officers against the risk of liabilities incurred in their capacity as directors and officers. It may also provide cover to the company taking the policy by way of reimbursement for amounts lawfully paid by the company to its directors and officers for such liabilities.

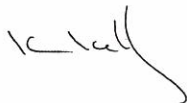
However, neither the Trade Practices Act nor the Bill has an equivalent to section 199B of the Corporations Act which sets out the liabilities for which a company cannot pay an insurance premium. The approach taken in the Corporations Act leaves it clear that a company can pay an insurance premium for the liabilities not set out in section 199B.

With attention focused by the new civil penalties, general insurers that offer D&O and their legal advisers are questioning whether, because of the absence of an equivalent to section 199B, the Bill precludes payment of premiums for D&O insurance which covers such liabilities. There is no apparent policy distinction which explains the different approach between the Corporations Act and the Trade Practices Act and the Australian Consumer Law.

The Insurance Council would appreciate the Committee seeking clarification of the intention behind the legislative approach adopted in the Bill to the prohibition of indemnification of officers. As the Committee will recognise, depending on the outcome Insurance Council members may need to amend existing as well as future D&O policy wordings. This would have significant legal and cost implications for both insureds and insurers and should only be required if there is a strong policy justification.

If you require any further information on these matters, please contact John Anning, Insurance Council's General Manager, Policy – Regulation Directorate on (02) 9253 5121, or at janning@insurancecouncil.com.au

Yours sincerely



Kerrie Kelly
Executive Director & CEO

TRADE PRACTICES ACT 1974

77A Indemnification of officers

- (1) A body corporate (the **first body**), or a body corporate related to the first body, must not indemnify a person (whether by agreement or by making a payment and whether directly or through an interposed entity) against any of the following liabilities incurred as an officer of the first body:
- (a) a civil liability;
 - (b) legal costs incurred in defending or resisting proceedings in which the person is found to have such a liability.

Penalty: 25 penalty units.

- (2) For the purposes of subsection (1), the outcome of proceedings is the outcome of the proceedings and any appeal in relation to the proceedings.

Definitions

- (3) In this section:

civil liability means a liability to pay a pecuniary penalty under section 76 for a contravention of a provision of Part IV.

officer has the same meaning as in the *Corporations Act 2001*.

77B Certain indemnities not authorised and certain documents void

- (1) Section 77A does not authorise anything that would otherwise be unlawful.
- (2) Anything that purports to indemnify a person against a liability is void to the extent that it contravenes section 77A.

77C Application of section 77A to a person other than a body corporate

If, as a result of the operation of Part 2.4 of the *Criminal Code*, a person other than a body corporate is:

- (a) convicted of an offence (the **relevant offence**) against subsection 77A(1) of this Act; or
- (b) convicted of an offence (the **relevant offence**) against section 11.4 of the *Criminal Code* in relation to an offence referred to in subsection 77A(1) of this Act;

the relevant offence is taken to be punishable on conviction by a fine not exceeding 5 penalty units.

CORPORATIONS ACT 2001

Part 2D.2—Restrictions on indemnities, insurance and termination payments

Division 1—Indemnities and insurance for officers and auditors

199A Indemnification and exemption of officer or auditor

Exemptions not allowed

- (1) A company or a related body corporate must not exempt a person (whether directly or through an interposed entity) from a liability to the company incurred as an officer or auditor of the company.

When indemnity for liability (other than for legal costs) not allowed

- (2) A company or a related body corporate must not indemnify a person (whether by agreement or by making a payment and whether directly or through an interposed entity) against any of the following liabilities incurred as an officer or auditor of the company:
- (a) a liability owed to the company or a related body corporate;
 - (b) a liability for a pecuniary penalty order under section 1317G or a compensation order under section 1317H or 1317HA;
 - (c) a liability that is owed to someone other than the company or a related body corporate and did not arise out of conduct in good faith.

This subsection does not apply to a liability for legal costs.

When indemnity for legal costs not allowed

- (3) A company or related body corporate must not indemnify a person (whether by agreement or by making a payment and whether directly or through an interposed entity) against legal costs incurred in defending an action for a liability incurred as an officer or auditor of the company if the costs are incurred:
- (a) in defending or resisting proceedings in which the person is found to have a liability for which they could not be indemnified under subsection (2); or
 - (b) in defending or resisting criminal proceedings in which the person is found guilty; or
 - (c) in defending or resisting proceedings brought by ASIC or a liquidator for a court order if the grounds for making the order are found by the court to have been established; or
 - (d) in connection with proceedings for relief to the person under this Act in which the Court denies the relief.

Paragraph (c) does not apply to costs incurred in responding to actions taken by ASIC or a liquidator as part of an investigation before commencing proceedings for the court order.

Note 1: Paragraph (c)—This includes proceedings by ASIC for an order under section 206C, 206D, 206E or 206EAA (disqualification), section 232 (oppression), section 1317E, 1317G, 1317H or 1317HA (civil penalties) or section 1324 (injunction).

Note 2: The company may be able to give the person a loan or advance in respect of the legal costs (see section 212).

- (4) For the purposes of subsection (3), the outcome of proceedings is the outcome of the proceedings and any appeal in relation to the proceedings.

199B Insurance premiums for certain liabilities of director, secretary, other officer or auditor

- (1) A company or a related body corporate must not pay, or agree to pay, a premium for a contract insuring a person who is or has been an officer or auditor of the company against a liability (other than one for legal costs) arising out of:
- (a) conduct involving a wilful breach of duty in relation to the company; or
 - (b) a contravention of section 182 or 183.

This section applies to a premium whether it is paid directly or through an interposed entity.

- (2) An offence based on subsection (1) is an offence of strict liability.

Note: For ***strict liability***, see section 6.1 of the *Criminal Code*.

199C Certain indemnities, exemptions, payments and agreements not authorised and certain documents void

- (1) Sections 199A and 199B do not authorise anything that would otherwise be unlawful.
- (2) Anything that purports to indemnify or insure a person against a liability, or exempt them from a liability, is void to the extent that it contravenes section 199A or 199B.