

Chapter 4

Codes of practice

Introduction

4.1 One of the key issues considered in this report is appropriate industry regulation. The notion of a code of practice for the life insurance industry is a recent phenomenon with the Financial Services Council (FSC) instigating a self-regulatory code for its members and the Insurance in Superannuation Working Group (ISWG) developing a draft code of practice for superannuation trustees and insurers.

4.2 However, serious questions arose during this inquiry as to whether industry codes based on self-regulation are in fact sufficient to prevent poor practices. Consequently, several submitters and witnesses favoured a co-regulatory model which, they argued, had far greater potential to not only facilitate best-practice in the life insurance industry, but also to restore consumer confidence in the sector.

4.3 This chapter covers codes of practice in the life insurance industry and:

- summarises codes of practice across the financial services sector;
- examines the use of codes of practice in the life insurance sector to date;
- considers evidence received during the inquiry on codes of practice; and
- considers the co-regulatory model proposed by the ASIC Enforcement Review Taskforce.

Terminology

4.4 During the inquiry submitters and witnesses used the terms 'code of practice' and 'code of conduct' interchangeably. This report uses the term code of practice, except where evidence referring to a code of conduct is quoted.

Financial services codes of practice

4.5 Codes of practice have existed in the financial services sector since the late 1980s. Most of these industry-based codes were voluntary for industry participants. The codes aimed, on the one hand, to provide flexibility to industry participants, and on the other hand, to protect consumers of financial products and services through the setting of best practice standards of conduct and providing a system of informal dispute resolution.¹

4.6 Regulatory Guide 183 *Approval of financial service sector codes of conduct* (RG183) sets out requirements for a code to be approved by ASIC under the Corporations Act. RG183 includes requirements for the code to be written in plain

1 ASIC Enforcement Review Taskforce, *Position and Consultation Paper 4 Industry Codes on the Financial Sector*, 28 June 2017, pp. 1, 4.

language, to address stakeholder issues, to provide for consistent monitoring and compliance, and for mandatory three-year code reviews.²

4.7 Currently, there are 11 codes for financial services including banking, insurance, financial planning, brokering, and ePayments.³

4.8 The only self-regulatory code to be approved by ASIC is the Financial Planning Association's Professional Ongoing Fees Code.⁴

Life insurance codes of practice

4.9 The committee received evidence that a self-regulatory voluntary life insurance industry code of practice was established in 1995 and an HIV/AIDS life insurance code of practice was established in 1998. Apparently, neither code was embraced by the life insurance industry and, consequently, both codes fell into disuse.⁵

4.10 In 2015, the Trowbridge Review of Retail Life Insurance Advice recommended that a life insurance code be developed and modelled on the General Insurance Code of Practice and aimed at settings standards of best practice for life insurers, licensees and advisers (Policy Recommendation 6).⁶

4.11 The FSC led the development of the Life Insurance Code of Practice (Code). The Code came into effect from 11 October 2016 and all FSC life insurer members (which does not include all industry participants) were bound by the Code from 1 July 2017.⁷

4.12 The FSC has over 100 members from Australia's retail and wholesale funds management businesses, superannuation funds, life insurers, financial advisory networks and licensed trustee companies.⁸ The FSC website indicates that 22 life insurance companies are members and are bound by the Life Insurance Code of

2 ASIC Enforcement Review Taskforce, *Position and Consultation Paper 4 Industry Codes on the Financial Sector*, 28 June 2017, p. 5.

3 ASIC Enforcement Review Taskforce, *Position and Consultation Paper 4 Industry Codes on the Financial Sector*, 28 June 2017, p. 5.

4 ASIC Enforcement Review Taskforce, *Position and Consultation Paper 4 Industry Codes on the Financial Sector*, 28 June 2017, p. 5.

5 Berrill & Watson Lawyers, *Submission 19*, pp. 1–2.

6 Mr John Trowbridge, *Review of Retail Life Insurance Advice*, March 2015, p. 10.

7 Financial Services Council, *Submission 26*, pp. 1, 6; ASIC Enforcement Review Taskforce, *Position and Consultation Paper 4 Industry Codes on the Financial Sector*, 28 June 2017, p. 4.

8 Financial Services Council, *FSC full members*, <https://www.fsc.org.au/about/fsc-members/> (accessed 7 February 2018).

Practice from 30 June 2017.⁹ There are currently 29 life insurers registered in Australia under section 21 of the *Life Insurance Act 1995*.¹⁰

4.13 The Code will be subject to an independent governance framework through the Life Code Compliance Committee (LCCC). The LCCC includes three independent experts including a consumer advocate. The LCCC is able to require life insurers who do not comply with the Code to take corrective action and be subject to sanctions.¹¹ Sanctions may include:

- a requirement that particular rectification steps be taken within a specified timeframe, taking into account any rectification related to the breach imposed by any regulatory body;
- a formal warning;
- a requirement that a code compliance audit be undertaken;
- a requirement to undertake corrective advertising or write directly to the customers impacted by the breach; and/or
- publication of non-compliance on the company's own website and on the FSC website.¹²

4.14 The Code covers customer service, plain language disclosure, updating medical definitions, conduct and monitoring of sales, remedies for mis-selling, claims handling, claims investigations, interviews and surveillance. The Code requires:

- prescribed timeframes for deciding claims;
- insurers to keep customers informed about the process and progress of a claim;
- insurers to provide reasons for information requests;
- alternative methods of verifying information prior to arranging surveillance and that surveillance be discontinued where there is evidence from an independent medical examiner that it negatively impacts the claimant's recovery;
- monitoring of sales practices and the offer of remedies, such as refund or replacement policy, where the insurer discovers that an inappropriate sale has occurred; and
- reviews of key medical definitions every three years.¹³

9 Financial Services Council, *Code of Practice*, <https://www.fsc.org.au/policy/life-insurance/code-of-practice/> (accessed 7 February 2018).

10 Australian Prudential Regulation Authority, *Registered Life Insurance Companies*, <http://www.apra.gov.au/lifs/Pages/registered-life-insurers.aspx> (accessed 7 February 2018).

11 Financial Services Council, *Submission 26*, p. 10.

12 Financial Service Council, *Life insurance Code of Practice*, p. 26.

13 Financial Services Council, *Submission 26*, p. 10.

4.15 The above Code did not extend to superannuation trustees involved with group life insurance. In response to that concern, the Insurance in Superannuation Working Group (ISWG) was established to develop a code of practice for superannuation trustees and insurers.¹⁴

4.16 In September 2017, the ISWG released a draft Insurance in Superannuation Code of Practice (Super Code) to apply to superannuation funds that offer insurance. The draft Super Code includes:

- Benefit design: to ensure automatic insurance benefits are appropriate and affordable for all segments of members, notably younger members, those making low or infrequent contributions, as well as those nearing retirement.
- Premium limits: trustees to design benefits to ensure the level and cost of cover does not exceed 1 per cent of estimated earnings and 0.5 per cent for members under 25.
- Cessation arrangements: to come into effect only after communicating with members; insurance premiums will stop being deducted 13 months after a member's contributions cease.
- Duplicate insurance cover: trustees required to ask new members for permission to help them identify any other insurance cover held within superannuation.
- Member communication initiatives: to assist members to understand what insurance products they hold and the impact insurance premiums can have on their retirement savings.
- Better claims handling initiatives: to include response times and better information provided to members.¹⁵

4.17 Mr David Haynes, Executive Manager for Policy and Research at the Australian Institute of Superannuation Trustees, informed the committee that the Super Code should lead to substantive improvements in the provision of life insurance within superannuation. For example, in areas such as claims handling, there will be an enforceable code to which the whole of the industry signs up and which is then endorsed and effectively overseen by ASIC.¹⁶

4.18 During the course of the inquiry, the draft Super Code was proceeding through a consultation and review process. The Super Code is intended to bind superannuation fund trustees that offer insurance within an APRA-regulated superannuation fund. The ISWG is currently contemplating options (including regulatory options) for ensuring the Super Code is mandatory for all superannuation

14 ASIC Enforcement Review Taskforce, *Position and Consultation Paper 4 Industry Codes on the Financial Sector*, 28 June 2017, p. 7.

15 Insurance in Superannuation Working Group, *Super industry consults on draft Code of Practice to improve outcomes for members*, 20 September 2017, pp. 7–12.

16 Mr David Haynes, Executive Manager Policy and Research, Australian Institute of Superannuation Trustees, *Committee Hansard*, 22 February 2017, p. 57.

trustees, in order to achieve broad industry change. The ISWG is also considering whether the two life insurance codes of practice—that is the FSC-coordinated Code and the ISWG-coordinated Super Code—could be combined.¹⁷

4.19 The final ISWG Super Code was released in December 2017 and takes effect from 1 July 2018.¹⁸ As the final version of the code was released well after the committee had received submissions and taken evidence during hearings, the committee's report has made reference to evidence it received on the draft ISWG Super Code.

4.20 The FOS acknowledged that while there may be technical difficulties in establishing a single life insurance code that would be far preferable to multiple codes which may add to complexity for consumers and difficulties in ensuring consistent standards across the industry for subscribers.¹⁹

Evidence received on life insurance codes of practice

4.21 The FSC submitted that the Code sets standards above existing laws in many areas. As such, the FSC argued that the Code is intended to strengthen industry standards for the benefit of all Australians.²⁰

4.22 Under the current self-regulatory model, the codes are voluntary and are not approved by ASIC. While a code could be approved by ASIC, ASIC would not have the power to enforce the code, which can be monitored by the LCCC. In this regard, Mr Peter Kell, Deputy Chairman of ASIC, observed:

The industry has also indicated to us that their intention is to submit the code for our approval. That doesn't necessarily mean that ASIC would enforce all the provisions, but we would only approve it if we were confident that the enforceability was robust.²¹

4.23 BT Financial supported the Code, informing the committee that in its view, the measures will foster trust, transparency and accountability across all aspects of the life insurance industry.²²

4.24 FOS supported recent industry initiatives to develop the Code. FOS noted, however, that a code is only as good as its implementation. FOS therefore emphasised

17 Insurance in Superannuation Working Group, *Consultation Paper: Insurance in Superannuation Code of Practice*, September 2017, pp. 5–6.

18 Insurance in Superannuation Working Group, *Insurance in superannuation voluntary code of practice*, December 2017.

19 Financial Ombudsman Service Australia, *Submission 28*, p. 14.

20 Financial Services Council, *Submission 26*, p. 1.

21 Mr Peter Kell, Deputy Chairman, Australian Securities and Investments Commission, *Committee Hansard*, 8 September 2017, p. 55.

22 BT Financial, *Submission 13*, p. 1.

the importance of clear communication to policy holders and consumers about the content of the Code, and in particular, the processes relating to claims assessment.²³

4.25 The FOS also suggested improvements in the next version of the Code including:

- covering all services provided by life insurers;
- holding subscribers accountable for the actions and conduct of employees;
- timeframes for handling complaints;
- standardising medical definitions where appropriate;
- a single uniform approach to the cancellation of policies for non-payment of premiums; and
- making the code easier for consumers to understand.²⁴

4.26 FOS also argued that the Code should become part of the contract with the consumer, and also that the code should be approved by ASIC:

What we would say about the code, for example, is that it currently does not form part of the contract between the applicant or the insured and the insurer and that perhaps, going forward in the second iteration, that is something that could indeed occur. We feel that that would allow the individuals who have rights under the code to enforce them more sufficiently. We also understand that the FSC is looking to have that code approved. Again, we feel that that is a good step because it will send a message to consumers that the code can be trusted and that it will be enforced and monitored, and that life insurers will be held accountable, as they should be, under the code.²⁵

4.27 Consumer groups and lawyers were critical of shortcomings in the Code. In particular, there was a broad recognition from consumer groups, lawyers, and FOS that the Code must be registered with ASIC in order to increase its effectiveness.²⁶

4.28 Maurice Blackburn Lawyers argued that a self-regulated code is insufficient, and represents a wasted opportunity to effect genuine change in the industry. In addition, Maurice Blackburn Lawyers suggested that the Code should:

- regulate the conduct of insurance companies in assessing claims;
- provide for the fair and reasonable exchange of documentation relied upon in assessing claims; and

23 Mr Shane Tregillis, Chief Ombudsman, Financial Ombudsman Service Australia, *Committee Hansard*, 22 February 2017, p. 61.

24 Financial Ombudsman Service Australia, *Submission 28*, pp. 14–15.

25 Dr June Smith, Lead Ombudsman, Investment and Advice, Financial Ombudsman Service Australia, *Committee Hansard*, 22 February 2017, p. 66.

26 Consumer Action Law Centre, *Submission 27*, p. 12; Financial Rights Legal Centre, *Submission 17*, p. 7; Financial Ombudsman Service, *Submission 28*, p. 13; Australian Lawyers Alliance, *Submission 20*, p. 24.

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- include hard time frames so that claims are assessed in a timely manner.²⁷

4.29 The FRLC stated that the Code does not meet best practice standards and does little, if anything, to restore confidence in the industry. The FRLC argued for greater oversight by ASIC to bring the industry into line with community standards.²⁸

4.30 The FRLC also had concerns about the process in the Code for updating medical definitions:

Central to our concerns is that the 'relevant' medical specialist does not have to be independent of the insurers. Who is a 'relevant' medical specialist is entirely at the discretion of insurers and the FSC. This fundamentally undermines the appearance of impartiality and raises questions as to the validity of the draft and any review into medical definitions, in the eyes of consumers.²⁹

4.31 The Consumer Action Law Centre acknowledged that the Code may lead to improved claims handling timeframes and greater protections for policyholders during investigations and surveillance processes.

4.32 However, Consumer Action Law Centre also pointed to significant weaknesses in the Code, including that:

- the Code is not enforceable by courts or tribunals, or registered with ASIC;
- the claims timeframes do not apply to people who have life insurance in their superannuation, which is the majority of life insurance; and
- the three-yearly reviews by a 'relevant' medical specialist do not have to be undertaken independently of the insurers. The Code also only guarantees some updates to medical definitions for 'on sale' policies only, excluding the many people whose policies are no longer 'on sale'.³⁰

4.33 Likewise, the Australian Lawyers Alliance (ALA) identified significant shortcomings in the Code, including that it:

- does not do enough to protect the rights and interests of consumers;
- provides no real remedy for its breach and therefore no incentive for compliance;
- has limited scope and coverage; and
- does not cover all participants in the industry.³¹

27 Maurice Blackburn Lawyers, *Submission 12*, pp. 15–16.

28 Financial Rights Legal Centre, *Submission 17*, p. 8.

29 Financial Rights Legal Centre, *Submission 17*, pp. 8–9.

30 Consumer Action Law Centre, *Submission 27*, p. 11.

31 Australian Lawyers Alliance, *Submission 20*, p. 24.

4.34 The ALA was also critical of the role of the LCCC because the LCCC cannot take any direct action to assist a consumer who may be the victim of a breach of the Code. While, the LCCC can impose rectification steps, they are not defined. Indeed, the ALA argued that the strongest identified sanction that can be imposed by the LCCC is that the insurer will have to write to the consumer about the issue.³²

4.35 While the vast bulk of the evidence to the committee argued that the Code was weak, limited in scope, and should be approved by ASIC, at the other end of the spectrum, one submitter did not support the Code because, in their view, the Code was unnecessary and went too far. That submitter argued that the Code would drive up premiums, reduce the adviser network, and cause even greater levels of under-insurance in Australia.³³

ASIC Enforcement Review Taskforce—Co-regulation

4.36 In October 2016, the government announced an ASIC Enforcement Review Taskforce (Taskforce) to review the adequacy of ASIC's enforcement regime, including in relation to codes of practice.³⁴

4.37 In June 2017 the Taskforce released a consultation paper on industry codes in the financial sector. The consultation paper considered the merits of self-regulatory and co-regulatory approaches:

The impact on the lives of those affected by poor practices, as brought to light in media reports and in Parliamentary and other inquiries, has resulted in the Australian financial sector coming under intense public and regulatory scrutiny in recent times and in the impairment of consumer confidence in the sector. In this context it is apt to consider whether self-regulatory initiatives such as industry codes are achieving their potential, and whether that potential could better be achieved by the introduction of a co-regulatory model – at least for codes in relation to key services provided to retail and small business customers.³⁵

4.38 The Taskforce observed that where self-regulation is non-existent or has proved ineffective, and a legislative solution is not appropriate, co-regulation could significantly improve the content, consistency and enforceability of codes.³⁶

4.39 While the content of the code and the rules regulating industry behaviour are still determined by the industry participants, a co-regulatory model is a stronger form

32 Australian Lawyers Alliance, *Submission 20*, p. 25.

33 Rate Detective, *Submission 56*, p. 2.

34 The Hon Kelly O'Dwyer MP, Minister for Revenue and Financial Services, Media Release, *ASIC Enforcement Review Taskforce*, 19 October 2016, <http://kmo.ministers.treasury.gov.au/media-release/104-2017/> (accessed 8 November 2017).

35 ASIC Enforcement Review Taskforce, *Position and Consultation Paper 4 Industry Codes on the Financial Sector*, 28 June 2017, p. 1.

36 ASIC Enforcement Review Taskforce, *Position and Consultation Paper 4 Industry Codes on the Financial Sector*, 28 June 2017, p. 16.

of regulation than self-regulation because a co-regulatory code requires approval by ASIC, participation is mandatory, and the code is enforceable.

4.40 The introduction of an enforceable co-regulatory code in appropriate parts of the financial sector could boost consumer confidence in financial services.³⁷

4.41 The Taskforce consultation paper proposed a co-regulatory model for the financial services sector with the following components:

- The content and governance arrangements for relevant codes should be subject to approval by ASIC.
- Entities engaging in activities covered by an approved code should be required to subscribe to that code.
- Approved codes should be binding and enforceable against subscribers by contractual arrangements with a code monitoring body.
- An individual customer should be able to seek appropriate redress through the subscriber's internal and external dispute resolution arrangements for non-compliance with an approved code.
- The code monitoring body, comprising a mix of industry, consumer and expert members, should monitor the adequacy of the code and industry compliance with it over time, and periodically report to ASIC on these matters.³⁸

4.42 The Taskforce considered that the proposed co-regulatory approach should apply to sectors of the industry that would be covered by an external dispute resolution body such as the proposed Australian Financial Complaints Authority (AFCA).³⁹

4.43 If a consumer lodged a complaint about an insurer's compliance with the code, the external dispute resolution body would apply the code of practice to any dispute between the insurer and the insured.⁴⁰

4.44 As noted above, codes may also give rise to enforceable rights in court actions as codes may form part of the contract between the parties. In addition, the ASIC Act

37 ASIC Enforcement Review Taskforce, *Position and Consultation Paper 4 Industry Codes on the Financial Sector*, 28 June 2017, p. 1.

38 ASIC Enforcement Review Taskforce, *Position and Consultation Paper 4 Industry Codes on the Financial Sector*, 28 June 2017, pp. 1–2.

39 ASIC Enforcement Review Taskforce, *Position and Consultation Paper 4 Industry Codes on the Financial Sector*, 28 June 2017, pp. 2, 6.

40 Mr Michael Sadaat, Senior Executive Leader, Deposit Takers, Credit and Insurers, Regional Commissioner, New South Wales, Australian Securities and Investments Commission, *Committee Hansard*, 8 September 2017, p. 55.

provides that a court may have regard to an industry code in determining whether the conduct of a financial services supplier is unconscionable.⁴¹

4.45 The Electronic Funds Transfer Code of Practice (now known as the ePayments code) is the only co-regulatory code currently operating in the retail financial services system.⁴²

Committee view

4.46 The committee notes that while the Financial Services Council argued that the Life Insurance Code of Practice set standards above current legislative requirements, consumer groups argued that the Code falls well short of best practice and some community expectations.

4.47 Furthermore, the Insurance in Superannuation Working Group has only just released a code of practice for superannuation trustees and insurers. Given that most life insurance is held in superannuation, the committee considers this to be a somewhat tardy response to a pressing issue. In addition, there is no mechanism for ASIC or a consumer to enforce the present industry Code, or to seek compensation.

4.48 The committee has considered the current self-regulatory approach adopted by the Financial Services Council and the Insurance in Superannuation Working Group. The committee is not persuaded that the current voluntary approaches to industry self-regulation put forward by the Financial Services Council and Insurance in Superannuation Working Group are sufficient to deter misconduct and address the poor practices that have become all too prevalent in the life insurance industry.

4.49 The committee also notes that previous self-regulatory codes in the life insurance industry fell into disuse. The committee considers that it would be unacceptable for such a situation to recur.

4.50 In light of the above, the committee welcomes the co-regulatory approach proposed by the ASIC Enforcement Review Taskforce. The committee is persuaded that co-regulation would have greater potential to foster best-practice in the life insurance industry and, as a consequence, help restore much-needed consumer confidence in the sector.

4.51 In particular, the committee considers that, with respect to the life insurance industry, a co-regulatory approach must, at a minimum, deliver a code that:

- is written in plain English that regulates the conduct of life insurance companies in assessing claims;
- is mandatory for all industry participants;
- is registered with ASIC;

41 ASIC Enforcement Review Taskforce, *Position and Consultation Paper 4 Industry Codes on the Financial Sector*, 28 June 2017, p. 6.

42 ASIC Enforcement Review Taskforce, *Position and Consultation Paper 4 Industry Codes on the Financial Sector*, 28 June 2017, pp. 1, 4.

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- is enforceable in order to create accountability; and
 - provides genuine remedies for its breach, including financial remedies, thereby creating an incentive for compliance.

Recommendation 4.1

4.52 The committee recommends that the government implement the co-regulatory approach put forward in the ASIC Enforcement Review Taskforce Position Paper across the whole financial services sector, while ensuring, where possible, that there are no exemptions for any part of the life insurance industry and that codes are written in plain English.

4.53 The co-regulatory approach would give the code compliance committees the power to determine whether breaches had occurred and the Australian Financial Complaints Authority the power to enforce compliance through determinations. However, both those processes only generally relate to individual breaches of codes, as they are unlikely to be effective in addressing systemic or systematic breaches of codes.

4.54 As a matter of practice, ASIC focusses its activities on systemic and systematic misconduct. However, under the proposed arrangements, ASIC may not have the power to undertake enforcement action for systemic and systematic code breaches. This would result in a very significant gap in consumer protections.

4.55 In its recent inquiry into Whistleblower Protections, the committee's recommendation 5.2 would include breaches of industry codes within the definition of disclosable conduct.⁴³

4.56 In other words, if that particular recommendation was implemented, whistleblowers would receive protection for blowing the whistle about serious misconduct such as systemic or systematic breaches of codes of practice. This may allow a company to receive and take action in relation to such a disclosure. However, under the proposed co-regulatory model a regulator, such as ASIC, would not have the power to take effective enforcement action in relation to the disclosure.

4.57 The committee therefore considers that it is essential for regulators to have appropriate enforcement powers in relation to systemic or systematic breaches of industry codes of practice in addition to the proposed co-regulatory model.

Recommendation 4.2

4.58 The committee recommends that ASIC be given the power to undertake enforcement action (halting misconduct, remedies and sanctions) in relation to systemic or systematic breaches of codes of practice in the financial services sector, including in the life insurance sector.

4.59 The committee also notes that the Life Insurance Code of Practice does not place obligations on financial advisers or planners selling or advising on life

43 Parliamentary Joint Committee on Corporations and Financial Services, *Whistleblower Protections*, September 2017, p. xiii.

insurance. This is another in a very long list of exemptions from adequate consumer protections that the life insurance industry currently exploits. The committee considers the exemption to be a serious flaw, particularly given the poor conduct of some advisers identified in several recent inquiries and reviews.

4.60 The committee therefore considers that, in order for codes of practice in the financial services sector (including life insurance) to be approved by ASIC, they must apply to all relevant industry participants, without exceptions.

Recommendation 4.3

4.61 The committee recommends that, in order for ASIC to approve any code of practice in the financial services sector, including life insurance, the code must apply to all relevant industry participants, without exemptions.

4.62 Finally, the committee supports the view, put forward by the Financial Ombudsman Service amongst others, that it would be much easier for consumers for there to be a single life insurance code of practice. The committee therefore recommends that, prior to seeking ASIC approval, the Life Insurance Code of Practice and the Insurance in Superannuation Code of Practice be combined into a single code for the life insurance industry if possible.

Recommendation 4.4

4.63 The committee recommends that, prior to seeking ASIC approval, the two codes of practice for the life insurance industry be combined into a single code of practice if possible.