MARCH 2015

Corporations Amendment (Life Insurance Remuneration Amendments) Bill 2016

Submission to the Senate Economics Legislation Committee

ABOUT US

Set up by consumers for consumers, CHOICE is the consumer advocate that provides Australians with information and advice, free from commercial bias. By mobilising Australia's largest and loudest consumer movement, CHOICE fights to hold industry and government accountable and achieve real change on the issues that matter most.

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CHOICE welcomes the opportunity to provide comment on the Corporations Amendment (Life Insurance Remuneration Arrangements) Bill 2015 (the Bill).

The Bill places limits on how financial advisers arranging life insurance can be remunerated. It does this by removing the current exemption that allows advisers to receive commissions for life insurance products and enabling ASIC to determine acceptable remuneration arrangements. As announced by the Assistant Treasurer and Minister for Small Business, ASIC will cap upfront and trail commissions and introduce a two-year clawback requirement to reduce the risk of inappropriate product churn.[1]

This Bill will improve the situation for consumers but CHOICE is still concerned at ongoing issues in this market. As long as commissions and other sales incentives for financial advisers remain, consumers will not be able to trust the financial advice industry to help them find the right life insurance product for their needs.

CHOICE recommends that the Bill is passed without amendment and that further steps are taken to remove conflicted remuneration in the long-term. ASIC should commence work on a plan to phase out all commissions in life insurance advice for the benefit of consumers.

Commissions lead to consumer harm

There is clear evidence that advisers who receive commissions are more likely to recommend inappropriate products for their client and are more likely to switch a client into a new product unnecessarily.

A 2014 ASIC review of retail life insurance advice found high levels of churn across the industry, where clients are placed into new products. 37% of advice failed to prioritise the needs of the client and comply with the law. High upfront commissions are strongly correlated with poor advice; 45% of advisers who were paid through up front commissions failed to comply with the law.[2]

The ASIC report clearly found that high upfront commissions lead to the worst consumer outcomes. The report concluded that:

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[1] See http://parlinfo.aph.gov.au/parlInfo/search/display/display.w3p;query=Id%3A%22chamber%2Fhansardr%2F11a9f69e-a789-4d75-854d-edb89ae01a41%2F0029%22

[2] ASIC (2014), *Report 413: Review of retail life insurance advice*, pp. 5-7.

"High upfront commissions give advisers an incentive to write new business. The more premium they write, the more they earn. There is no incentive to provide advice that does not result in a product sale or to provide advice to a client that they retain an existing policy unless the advice is to purchase additional covers or increase the sum insured."[3]

Current remuneration arrangements encourage advisers to sell products rather than provide quality personal advice. Being sold an inappropriate life insurance product causes long-term financial and personal harm to consumers. It means consumers waste money on a product they can't use, and should something go wrong, they or their families are not covered as expected. Overtime, widespread misselling and poor behaviour from advisers means consumers lose trust in the financial system.

Given the harm that commissions cause consumers, CHOICE maintains that they should be banned in life insurance advice, just as they are for other kinds of advice. However, CHOICE recognises that this Bill and the related industry agreement is an improvement on the status quo.

There must be no further concessions on commissions and claw back arrangements

CHOICE views this Bill as the minimum change required to increase consumer confidence in the life insurance advice industry. Further reform is necessary and should be implemented in a staged manner over the coming years.

CHOICE asks the Committee to keep in mind the consultation process so far when considering this Bill. The initial proposals to reform life insurance remuneration have been watered down over the course of multiple inquiries.

Initially, the Financial System Inquiry proposed removing upfront commissions entirely to eliminate the most obvious conflict for advisers and reduce consumer churn. In response to the Financial System Inquiry and the ASIC Review of Retail Life Insurance Advice, industry groups commissioned an independent report (the Trowbridge Report) that called for some change to commissions and a significant intervention to prevent product churn through a single upfront payment per client every five years. Since the Trowbridge Report, the Government has made two announcements on life insurance remuneration reform, both of

[3] Ibid para 147.

which have included concessions to life insurance advisers. Various proposals to deal with adviser remuneration are detailed in the table below.

Table one: summary of recommendations on life insurance advice remuneration, 2014-2016

	Current arrangements	Financial System Inquiry, Final Report recommendations December 2014[4]	Trowbridge Report recommendations March 2015[5]	Initial Government proposal, June 2015[6]	Proposed arrangements, March 2016
Maximum upfront commissions	No cap, a standard commission is 120%[7]	Upfront commissions should not be greater than ongoing commissions but did not specify a cap.	$1,200 or 60% if annual premium is below $2,000	60% by 1 July 2018	60% by 1 July 2018
Ongoing commissions	No cap, a standard commission is 10%		20%	20%	20%
Mechanism to prevent churn	None		Initial Advice Payment restricted to one payment for each client every five years. Clawback in first year.	Clawback 100% of commission in year one, 60% in year two, 30% in year three.	Clawback 100% of commission in year one, 60% in year two.

At each stage of the process, life insurance advisers have called for higher upfront commission levels and reduction or removal of mechanisms to prevent product churn. CHOICE encourages the Committee to, at minimum, support the current proposal for a limit of 60% on upfront commissions, 20% for ongoing or trail commissions and a two-year staged clawback.

[4] Financial System Inquiry (2015), *Final Report*, http://fsi.gov.au/publications/final-report/chapter-4/align-interests/
[5] See John Trowbridge, (March 2015) Review of Retail Life Insurance Advice a.k.a. "Trowbridge Report", p 5. http://www.fsc.org.au/downloads/file/MediaReleaseFile/FinalReport-ReviewofRetailLifeInsuranceAdvice-FinalCopy(CLEAN).pdf
[6] http://jaf.ministers.treasury.gov.au/media-release/032-2015/
[7] See Trowbridge report p 5. http://www.fsc.org.au/downloads/file/MediaReleaseFile/FinalReport-ReviewofRetailLifeInsuranceAdvice-FinalCopy(CLEAN).pdf