

Title	Australia - Changes to the Duty of Disclosure relating to consumer contracts
Purpose	To inform the market of changes affecting insurance contracts emanating from reforms of the Duty of Disclosure in Australia
Type	Event
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Date	18 August 2021
Deadline	From 5 October 2021 all newly defined consumer insurance contracts must meet the new requirements
Related links	Financial Sector Reform (Hayne Royal Commission Response) Act 2020 Explanatory Memorandum Insurance Contracts Act Insurance Contracts Regulations 2017
Attachments	Further details on the Explanatory Memorandum to the FSA Act (attachment A)

Background

The principal legislation governing insurance contracts in Australia is the Insurance Contracts Act 1984 (Cth) (the IC Act) coupled with the Insurance Contracts Regulations 1985 (see [Market Bulletin Y4921](#)). Schedule 2 to the [Financial Sector Reform \(Hayne Royal Commission Response\) Act 2020](#) (the FSR Act) amends the IC Act to replace the existing “eligible contracts of insurance” Duty of Disclosure regime (s 21A and 21B IC Act) and misrepresentation provisions (s 23-27 IC Act) with a new regime for the newly defined concept of “consumer insurance contracts” (CIC). These are essentially insurance contracts where the insurance is obtained wholly or predominantly for the personal, domestic or household purposes of the insured, or the insurer opts into the CIC regime.

For CIC the insured will have a new duty to take reasonable care not to make a misrepresentation to the insurer before entering into the consumer insurance contract, subject to various qualifications (s 20B IC Act). This is similar to the UK model applied under s 2 of the Consumer Insurance (Disclosure and Representation) Act 2021. The new CIC duty applies to CIC entered into (including new business, variations, extensions, reinstatements and renewals) on or after 5 October 2021. Prior to 5 October 2021 the existing obligations apply unless an insurer chooses to opt in earlier by giving an insured notice that the contract is a CIC.

For non-CIC, there is no significant change to the existing Duty of Disclosure and obligations under s 21 and s 22 of the IC Act and misrepresentation provisions (s 23A - 27 of IC Act) that underwriters must currently comply with.

What are the CIC changes?

The changes introduce a new Division 1A in relation to “consumer insurance contracts: insured’s duty to take reasonable care not to make a misrepresentation” replacing the existing eligible insurance contracts regime under s 21A and s 21B. The new duty provides:

“20B The insured’s duty to take reasonable care not to make a misrepresentation

- (1) Subject to this Act, an insured has a duty to take reasonable care not to make a misrepresentation to the insurer before the relevant contract of insurance is entered into. *(this includes varying, extending or renewing or reinstating)*
- (2) Whether or not an insured has taken reasonable care not to make a misrepresentation is to be determined with regard to all the relevant circumstances.
- (3) Without limiting subsection (2), the following matters may be taken into account in determining whether an insured has taken reasonable care not to make a misrepresentation:
 - (a) the type of consumer insurance contract in question, and its target market;
 - (b) explanatory material or publicity produced or authorised by the insurer;
 - (c) how clear, and how specific, any questions asked by the insurer of the insured were;
 - (d) how clearly the insurer communicated to the insured the importance of answering those questions and the possible consequences of failing to do so;
 - (e) whether or not an agent was acting for the insured;
 - (f) whether the contract was a new contract or was being renewed, extended, varied or reinstated.
- (4) Any particular characteristics or circumstances of the insured of which the insurer was aware, or ought reasonably to have been aware, are to be taken into account in determining whether an insured has taken reasonable care not to make a misrepresentation.
- (5) The insured is not to be taken to have made a misrepresentation merely because the insured:
 - (a) failed to answer a question; or
 - (b) gave an obviously incomplete or irrelevant answer to a question.

- (6) To avoid doubt, a misrepresentation made fraudulently is made in breach of the duty to take reasonable care not to make a misrepresentation.”

A new section s 20C confirms that a statement with respect to the existence of a state of affairs that is made in or in connection with a contract of insurance; and made by or attributable to the insured; does not have effect as a warranty but has effect as though it were a statement made to the insurer by the insured during the negotiations for the contract but before it was entered into. This does not change the existing position.

There is no specific notice provision or prescribed form of notice for CIC as there is for non-CIC. Practically, a form of notice will still be required. In addition, the s 71 exemption on insurers giving a s 22 notice where a broker acts for the client (broker exemption) won't apply in relation CIC, only non-CIC.

What needs to be done?

1. Identify which contracts you issue are CIC.

A CIC will capture:

- insurance obtained wholly or predominantly for the personal, domestic or household purposes of the insured (s 11AB) (this is the purpose of the contracting insured only not third party beneficiaries that merely get access to cover under the IC Act – see s 11 and 48); or
- if the insurer gives the insured written notice before the contract is entered into that the contract is a consumer insurance contract.

The IC Act does not define the terms “personal, domestic or household purposes” or “wholly or predominantly” and they are likely to be given their plain meaning. If it is alleged in a proceeding in relation to a contract of insurance that the contract is a consumer insurance contract, it is presumed to be one unless the contrary is established. This new defined term is not the same as the “retail client” test under the Corporations Act 2001 (Cth) which triggers the Product Disclosure Statements (PDS) and other retail client obligations or the “prescribed contract” definition under the IC Act to which special provisions apply. This means non PDS products and non-standard insurance can be caught if they fall within the new definition.

The contract of insurance as a whole must be considered to determine if it is CIC or not (except to the extent that some cover within the contract is not caught by the Act at all, in which case only consider the covers caught by the Act (s 9(1A)-(1C)). If the insured is not buying the insurance wholly or predominantly for their personal, domestic or household purposes, the non-CIC regime applies unless the insurer opts in.

Where clients may or may not be caught by the CIC definition and an insurer does not want to have separate arrangements (i.e. CIC duty for CIC customers and non-CIC duty for non-CIC customers) the insurers may choose to opt-in to the CIC regime. However, insurers cannot opt out of the CIC regime.

2. Update procedures and documentation for CIC obligations

Whether the insured has taken reasonable care not to make a misrepresentation to an insurer will involve consideration of:

- *Whether a misrepresentation has in fact been made* – the insured is not to be taken to have made a misrepresentation merely because the insured failed to answer a question or gave an obviously incomplete or irrelevant answer to a question (s 20B(5)).

We note that s 20B(5) is a significant issue in relation to automatic renewals. Current renewal procedures which rely on a legally deemed “no change” response where no answer is received by the customer to questions or disclosure of past answers on renewal (s 21B(10)) will no longer apply. This means an “answer” from a consumer to a question will be required in some form or s 20B(5) will be triggered. No relief is currently expected.

- *If there is a misrepresentation, whether the misrepresentation was made fraudulently* – in which case it is taken to be a breach of the duty (s 20B (6));
- *In all other misrepresentation cases:*
 - *Whether or not an insured has taken reasonable care not to make the relevant misrepresentation* – this is to be determined with regard to all the relevant circumstances (s 20B (2)). There is no limitation on the range of matters that can be considered but the section lists examples of matters that would need to be considered (see s 20B (3) above).
 - *Any particular characteristics or circumstances of the insured of which the insurer was aware, or ought reasonably to have been aware (s 20B (4))*. This is specific to the actual insured.

The Explanatory Memorandum to the FSA Act provides guidance on each of these matters above which are areas insurers need to focus on. See **Attachment A** for more detail.

In short, the process the insured goes through with the insurer will be subject to scrutiny and depending on this process the insured may be subject to a higher or lesser duty of care. Special consideration will need to be given to the clarity and specificity of questions asked and what additional guidance or information could or should be provided in relation to the new duty to support any argument that a consumer has breached the duty.

Whilst there is no requirement for a Duty of Disclosure notice for CIC, as is the case under s 22 of the IC Act for non-CIC, insurers should be providing information to insureds on their duty so that they are properly informed on what is required of them. A failure to do so will affect the duty of care applied to the insured and any remedies that may be available to the insurer.

Current Australian Duty of Disclosure notices LMA9109, LMA9110, LMA9111, LMA9112 and LMA9113 must not be used for any general insurance contracts entered into, renewed or varied on or after 5 October 2021.

Managing agents and their coverholders will need to:

- Review and update documentation such as:
 - PDS or supplementary PDSs;

- policy wordings and endorsements/variation wordings not subject to a PDS that fall within the CIC definition;
 - telephone scripts;
 - applications/proposals;
 - renewal notices;
 - schedules/Certificates of Insurance/endorsements/variations; and
 - websites.
- Identify where any other form of Duty of Disclosure related information is provided in existing materials and procedures e.g. training, web content, brochures, Q&As, underwriting, claims handling and complaints manuals or procedures etc and update it to reflect the changes.

Remedies for a breach of CIC and non-CIC duty

The remedies in Division 3 of Part IV of the Insurance Contracts Act continue to be available to an insurer if an insured breaches:

- the new CIC duty; or
- the non-CIC duty (per s 20E-22) or makes a misrepresentation (per s 23A-27) which essentially remains unchanged from the current position.

S 28 of the IC Act sets out the remedies in relation to a general insurance contract. In seeking a remedy under s 28 the onus of proof is on the insurer to establish the relevant failure. No remedy arises if the insurer would have entered into the contract, for the same premium and on the same terms and conditions, even if the failure had not occurred. Where this is not the case:

- If the relevant failure was fraudulent, the insurer may avoid the contract. Under s 31 of the IC Act a court may disregard avoidance in certain circumstances; or
- If the insurer is not entitled to avoid the contract or, being entitled to avoid the contract has not done so, the liability of the insurer in respect of a claim is reduced to the amount that would place the insurer in a position in which the insurer would have been if the relevant failure had not occurred.

Further information

This communication is provided for information purposes and is not intended to be a substitute for appropriate legal advice.

If you have any queries regarding this communication, please contact:

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Attachment A

Explanatory Memorandum CIC - Relevant matters and particular characteristics or circumstances of the insured examples

The Explanatory Memorandum relevantly provides:

2.50 The list of matters reflects common scenarios of relations between the insurer and the insured that may be relevant in determining whether an insured has fulfilled the new duty. This list of matters is indicative and non-exhaustive. Other matters may also be taken into account when relevant.

2.51 Further, if the insurer was, or ought to have been, aware of particular characteristics or circumstances of the insured individual, these characteristics or circumstances must be taken into account in determining whether the insured has taken reasonable care not to make a misrepresentation to the insurer.

The type of consumer insurance contract in question and its target market

2.52 The type of consumer insurance contract and its target market may be taken into account when determining whether the insured took reasonable care not to make a misrepresentation to the insured. [Schedule 2, item 6, s 20B of the Insurance Contracts Act]

2.53 Consumer insurance contracts can vary widely. For instance, consumer insurance contracts can have different pricing mechanisms, payment arrangements, subject-matters and terms and be of different duration. They can be negotiated, standard-form, written, verbal, online or a mix of these contract types. Therefore, the type of insurance contract may affect what the insured is required to do to satisfy the new duty.

2.54 For example, if a consumer purchases a bespoke motor vehicle insurance contract that has unique terms, such as for an antique car, it is likely that, before the contract is entered into, the insurer would seek more detailed information about the consumer and their circumstances than if the consumer was purchasing a standard motor vehicle insurance contract.

2.55 Policies containing options and levels of cover may have a broad target market with narrower components within them. For example, if a consumer selects the wrong insurance cover when purchasing online (such as commercial insurance instead of residential insurance) this should be taken into account when considering whether the duty was met by the insured in answering questions in relation to that contract.

2.56 Similarly, consumer insurance contracts can have different target markets. For example, home contents insurance for rare or otherwise unusually valuable items may be targeted toward users' needs. When taking this matter into consideration, a target market determination made by the insurer in accordance with their design and distribution obligations under the Corporations Act should be taken into account.

Explanatory material or publicity produced or authorised by the insurer

2.57 Whether the insurer provided easily comprehensible, accessible material that explains the specific consumer insurance contract in question would generally be taken into account in determining whether the insured discharged their duty. If that material was ambiguous, the ambiguity would also be taken into account. [Schedule 2, item 6, s 20B of the Insurance Contracts Act]

2.58 Explanatory materials may include both written and non-written communications to convey the type of information that the insurer considers relevant.

How clear, and how specific, any questions asked by the insurer were

2.59 The clarity and specificity of questions asked by the insurer may be taken into account when determining whether the insured took reasonable care not to make a misrepresentation to the insurer. [Schedule 2, item 6, s 20B of the Insurance Contracts Act]

2.60 There is no express consequence for insurers asking an insured to answer questions of a general nature or questions that are unclear, confusing or ambiguous (as is the case with the existing disclosure requirements for eligible insurance

contracts). However, this would likely be taken into account in determining whether the insured has satisfied their duty to take reasonable care not to make a misrepresentation.

2.61 For example, it may generally be more difficult for an insured to answer:

- compound questions that are open-ended, general or long; or
- questions that are difficult to understand or interpret.

2.62 Therefore, when assessing this matter, the sort of things that would be taken into account may be the type of questions asked as well as the circumstances in which the questions are asked.

2.63 In this regard it is intended that on the renewal of an insurance contract, the new law would not prevent an insurer from providing the insured with a copy of information previously provided and asking them for details of any material changes.

How clearly the insurer communicated the importance of answering those questions (or the possible consequences of failing to do so)

2.64 How clearly the insurer communicated the importance of answering the questions, and the possible consequences of failing to do so, may be taken into account when determining whether an insured has taken reasonable care not to make a misrepresentation. This will also be relevant where the insurer did not communicate the importance (or the consequences) of answering the questions. [Schedule 2, item 6, s 20B of the Insurance Contracts Act]

2.65 Therefore, an insurer should give a clear explanation of the duty to take reasonable care not to make a misrepresentation and the consequences of a misrepresentation (including the remedies available to the insurer if the insured fails to take reasonable care) to the insured. This explanation can be given to the insured in the form that the insurer considers to be effective.

2.66 S 22 of the Insurance Contracts Act (which requires an insurer to inform the insured of the existing Duty of Disclosure in writing) does not apply to consumer insurance contracts. However, this does not change the insurer's obligation to give a clear explanation of the new duty to the insured. In addition, consistent with s 22, a failure by the insurer to fulfil those obligations will reduce the remedies available to the insurer in the event that the insured does make a misrepresentation.

Whether or not an agent was acting for the insured

2.67 Whether or not an agent (such as a financial advisor or insurance broker) was acting for the insured is one of the matters that is relevant in determining whether the insured has fulfilled the new duty to take reasonable care not to make a misrepresentation to the insurer. [Schedule 2, item 6, s 20B of the Insurance Contracts Act]

2.68 The appointment of an agent by the insured does not, by itself, change the insured's duty to take reasonable care not to make a misrepresentation to the insurer. However, depending on the nature of the agent's involvement, it may be a reason to expect the insured was informed about their duty to take reasonable care not to make a misrepresentation and what they need to do to discharge the duty.

Whether the contract was a new contract or was being renewed, extended, varied or reinstated

2.69 The circumstances of an insured entering into a new contract are different to those surrounding the renewal, extension, variation or reinstatement of a contract. This may be taken into account when considering whether the new duty has been fulfilled. [Schedule 2, item 6, s 20B of the Insurance Contracts Act]

2.70 The insurer should communicate with and provide information to the insured in circumstances when:

- a contract is being entered into for the first time; or
- a contract is being renewed, extended, varied or reinstated.

2.71 When entering into a contract for the first time, the insurer may need to take greater care to ensure that they have done what is necessary to satisfy themselves of their knowledge of the insured's position.

2.72 In contrast, when an insurance contract is being renewed, extended, varied or reinstated, it may be appropriate for the insurer to provide previously disclosed information to the insured and ask them for details of any material changes (along the lines of what is currently provided for under the existing s 21A and s 21B of the Insurance Contracts Act).

Any particular characteristics or circumstances of the insured of which the insurer was aware, or ought reasonably to have been aware, are to be taken into account in determining whether an insured has taken reasonable care not to make a misrepresentation

2.73 The insured should follow the insurer's guidance as to what needs to be disclosed. Guidance may include the type of information that might need updating and examples of information commonly overlooked by an insured consumer.

Particular characteristics or circumstances of the insured that are known by the insurer must be taken into account.

2.74 S 20B(3) of the Insurance Contracts Act sets out matters that, if relevant, may be taken into account in determining whether the insured has taken reasonable care not to make a misrepresentation to the insurer. This list of matters reflects common scenarios of relations between the insurer and the insured that may be relevant in determining whether an insured has fulfilled the new duty but is non-exhaustive. Other matters may also be taken into account when relevant.

2.75 In relation to matters taken into account under s 20B(2) and (3) of the Insurance Contracts Act, if the insurer was aware, or ought reasonably to have been aware, of particular characteristics or circumstances of the insured, those characteristics or circumstances must be taken into account in determining whether the insured has taken reasonable care not to make a misrepresentation to the insurer.

[Schedule 2, item 6, s 20B of the Insurance Contracts Act]

2.76 As a result, an insured will not be disadvantaged under the new duty even if they do not specifically disclose those particular characteristics or circumstances to the insurer.

2.77 This makes it clear that an assessment of whether an insured met the standard of the duty is not limited to the actions of the insured and may require consideration of the insurer's knowledge of the insured's circumstances and the actions taken by the insurer once made aware of that knowledge.

2.78 For example, where an insured requires special assistance in satisfying the requirements for an insurance application, and the insurer is aware of this, whether and how the insurer assisted the insured will be relevant in determining whether the standard of the new duty was met by the insured. (s 20B(4)).