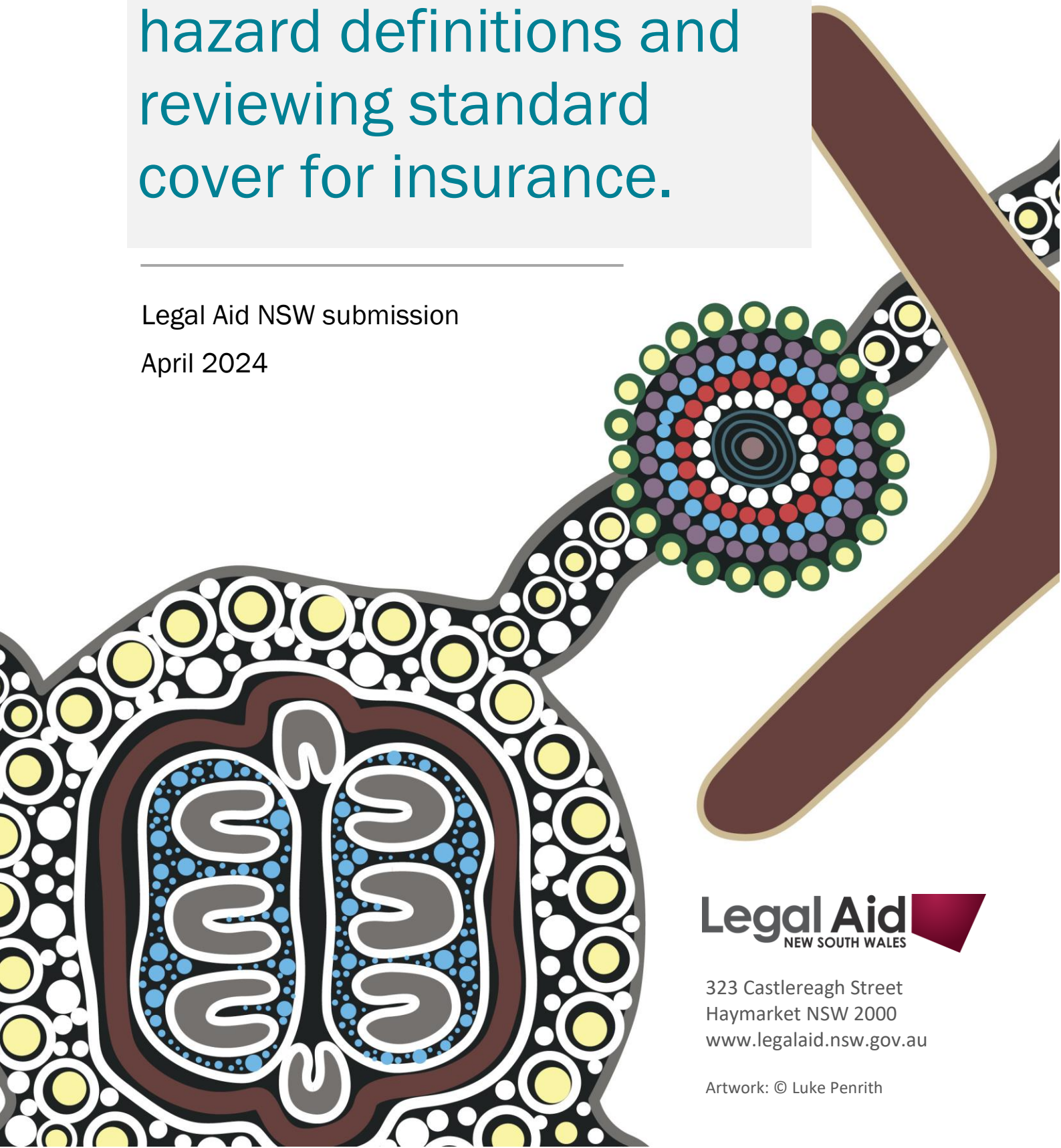


Treasury Consultation – Standardising natural hazard definitions and reviewing standard cover for insurance.

Legal Aid NSW submission

April 2024



Legal Aid
NEW SOUTH WALES

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Acknowledgement

We acknowledge the traditional owners of the land we live and work on within New South Wales. We recognise continuing connection to land, water and community.

We pay our respects to Elders both past and present and extend that respect to all Aboriginal and Torres Strait Islander people.

Legal Aid NSW is committed to working in partnership with community and providing culturally competent services to Aboriginal and Torres Strait Islander people.

About Legal Aid NSW

The Legal Aid Commission of New South Wales (**Legal Aid NSW**) is an independent statutory body established under the *Legal Aid Commission Act 1979* (NSW). We provide legal services across New South Wales through a state-wide network of 25 offices and 243 regular outreach locations, with a particular focus on the needs of people who are socially and economically disadvantaged. We offer telephone advice through our free legal helpline LawAccess NSW.

We assist with legal problems through a comprehensive suite of services across criminal, family and civil law. Our services range from legal information, education, advice, minor assistance, dispute resolution and duty services, through to an extensive litigation practice. We work in partnership with private lawyers who receive funding from Legal Aid NSW to represent legally aided clients.

We also work in close partnership with community legal centres, the Aboriginal Legal Service (NSW/ACT) Limited and pro bono legal services. Our community partnerships include 27 Women's Domestic Violence Court Advocacy Services, and health services with a range of Health Justice Partnerships.

The Legal Aid NSW Family Law Division provides services in Commonwealth family law and state child protection law.

Specialist services focus on the provision of family dispute resolution services, family violence services, services to Aboriginal families and the early triaging of clients with legal problems.

Legal Aid NSW provides duty services at all Family and Federal Circuit Court registries and circuit locations through the Family Advocacy and Support Services, all six

specialist Children's Courts, and in some Local Courts alongside the Apprehended Domestic Violence Order lists. Legal Aid NSW also provides specialist representation for children in both the family law and care and protection jurisdiction.

The Civil Law Division provides advice, minor assistance, duty and casework services from the Central Sydney office and most regional offices. The purpose of the Civil Law Division is to improve the lives of people experiencing deep and persistent disadvantage or dislocation by using civil law to meet their fundamental needs. Our civil lawyers focus on legal problems that impact on the everyday lives of disadvantaged clients and communities in areas such as housing, social security, financial hardship, consumer protection, employment, immigration, mental health, discrimination and fines. The Civil Law practice includes dedicated services for Aboriginal communities, children, refugees, prisoners, older people experiencing elder abuse and communities impacted by disasters.

The Criminal Law Division assists people charged with criminal offences appearing before the Local Court, Children's Court, District Court, Supreme Court, Court of Criminal Appeal and the High Court. The Criminal Law Division also provides advice and representation in specialist jurisdictions including the State Parole Authority and Drug Court.

Should you require any further information, please contact:

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Introduction

Legal Aid NSW (LANSW) welcomes the opportunity to make a submission to Treasury's consultation on standardising natural hazard definitions and reviewing standard cover for insurance.

While LANSW civil solicitors across the state do various insurance casework, most of our work in insurance has been a result of the catastrophic weather events over the last few years. This work is led by LANSW's specialist Disaster Response Legal Service (**DRLS**) which was established in early 2020 in response to the Black Summer Bushfires and provides statewide legal assistance, community legal education and information to individuals and communities impacted by disasters. The DRLS responded to all flood events within the scope of the current Flood Inquiry that occurred in NSW in 2022 and is the lead government agency coordinating the legal response to disasters in NSW.

From 1 March 2022 to 21 November 2023, the DRLS provided 6049 legal services to 3401 individuals impacted by the 2022 floods across 93 Local Government Areas. Of these services, 4205 were face to face services at Disaster Recovery Centres and Recovery Assistance Points across the state.

Insurance matters accounted for around 49 per cent of all legal services provided by the DRLS and in total 2984 services were about general insurance.

Consultation Questions

Standard definitions

1. To what extent is consumer misunderstanding of Insurance policies leading to unintentional underinsurance or inappropriate insurance?

In LANSW's experience, consumers are often only finding out about being underinsured or having inappropriate insurance at the time of lodging a claim. They are often surprised or shocked that the policy they have been paying for, in some cases for years, does not cover them for what they expected to be covered for.

Underinsurance and/or inappropriate insurance can be a result of several factors including:

1. The failure of the current standard cover regime in achieving its intended purpose which means that consumers do not have a base level of cover that they can effectively compare.
2. The varying definition of common terms across insurance policies causing confusion as to the extent of cover and also adding to the inability for effective comparison.
3. Consumers being overwhelmed with the multitude of complex insurance documentation (including PDS, supplementary PDS, key factsheets) which means they either struggle to understand the documents or simply do not engage with their insurance.
4. Lack of knowledge or understanding as to what appropriate insurance cover they need both in terms of the amount they need to be properly insured and what benefits are available under a policy.
5. Difficulty in assessing the appropriate sum insured amount where standards for rebuilding are unknown due to climate change, especially following bushfire events. This uncertainty can also be due to technological changes and market changes such as the cost of materials and trades.
6. Failure of insurers to properly engage consumers at renewal of a policy to review their cover resulting in sum insureds (and other policy limits) remaining the same for several years and eventually realising that they are underinsured when a claim is lodged.
7. The unaffordability of premiums resulting in significant portions of the community opting out of insurance entirely purely because they cannot afford it.

2. What are the consequences of not addressing these issues?

The consequences of not addressing these issues include:

- (a) Poor consumer outcomes, such as those highlighted in the current Flood Inquiry, will persist and may only increase.

- (b) Consumers will continue to be at risk of being underinsured and/or not being adequately protected particularly from the increasing number and severity of disasters impacting our community. This can mean that they won't be able to rebuild their homes to the same condition or sometimes at all.
 - (c) Consumers will not be able to effectively compare insurance products and select appropriate and affordable cover.
 - (d) Consumers will lose trust in insurance and may simply choose not to engage with insurance at all and ultimately relying on the government as the de facto insurer.
 - (e) Increase in poor health related outcomes for consumers particularly with stress and mental health issues following disasters and poor experience with their insurance claims. Consumers needing further health support and treatments puts further pressure on our health system.
 - (f) Social disruption if people are required to move away from their community and support networks which can lead to broader economic impacts.
3. [Aside from reviewing standard cover and standardising common terms, what other interventions may increase consumer understanding of insurance cover and reduce underinsurance or inappropriate insurance?](#)

Other interventions that may assist include:

(a) Transparency in premium pricing

Our clients often tell us that a major component of their decision-making process is the cost of insurance. At present, consumers don't really know how their premiums are calculated. They may receive some basic general information about what factors or components make up the price of their premiums but are regularly refused any specific information that would allow them to engage meaningfully with the process of deciding the appropriate level of cover for their needs. This also means they often don't have access to the best information available to help them assess the level of risk for their property, but this is information that is available to insurers. If premium pricing was transparent, consumers would have a better understanding of the risk for their property and what risk mitigation could reduce the cost of their premiums. This will also improve the trust between insureds and their insurer and could lead to more meaningful partnerships in risk mitigate and/or risk management.

(b) Meaningful discussions at the point of sale

Consumers often find out that they are either underinsured or have inappropriate insurance once they lodge a claim. This is obviously too late in the process for them and potentially could be avoided if there were meaningful discussions or engagement with their insurer at the point of sale. Insurers should encourage enquiries that lead to meaningful discussions whether consumers are purchasing policies over the phone or online. We consider that this is possible to do without the need for insurers to provide specific advice about the best cover for each individual

consumer as this would then be financial advice which they are prohibited from providing.

Consumers would benefit from meaningful discussions around the additional benefits under their policy, how limits are applied and how the premiums have been calculated. This should also extend to the full cycle of an insurance claim with insurers being required to proactively engage with insureds to ensure that they fully understand their entitlements under their policy and that all relevant entitlements are made available to them.

(c) Addressing poor communication practices

Our clients regularly tell us about the poor or ineffective communication practices of their insurer from inception of their policy, during the term of their policy but particularly following a claim. This has been a reoccurring theme during the current Flood Inquiry where evidence of the devastating impacts has been presented. We consider that such overwhelming evidence warrants a closer look at and examination of these poor communication practices to identify where there could be improvements that could result in better consumer outcomes.

4. Do you agree with the priority terms that are proposed for standardisation (fire, storm, stormwater, and rainwater run-off)?

LANSW agrees with the priority terms that are proposed for standardisation and appreciates that this is the starting point for the review, noting that it's our position that standardisation of all key terms that are prescribed by standard cover should be considered. Limiting the scope of terms to be standardised invites the possibility of other terms in a policy to be drafted in a manner that could lead to further confusion for consumers.

Currently, *flood* is the only natural hazard term that has been standardised. While our experience is that having a standard definition of flood reduced confusion in the community, avoiding a repeat of the 2010-2011 consumer experience in relation to floods, the fact that other key terms were not also standardised meant that the source of confusion simply shifted as definitions of other natural hazard terms varied. This was highlighted by a particular insurance policy that combined rainwater run-off exclusion with flood cover exclusion. Many of our clients were caught off-guard by this and were shocked to find out at the time of lodging their claim that in opting out of the flood cover they also inadvertently opted out of rainwater run-off cover.

Case study – Lisa's story

Lisa held both home building and contents insurance with the same insurer for more than 50 years and had been a loyal customer. The insurer purported to have sent notification to her in 2018 about changes to her insurance policy which effectively bundled storm surge and rainwater run-off with flood cover where opting out of the

flood cover would automatically include opting out of any cover for both storm surge and rainwater run-off. Lisa doesn't recall receiving this notice but does recall that her premiums increased in 2018 and she had contacted her insurer about this. The increase was partly due to the flooding events in the Northern Rivers in 2017. Lisa sought to reduce her premiums as her property had not been impacted by the 2017 floods or any time prior. Lisa recalled the insurer's representative saying words along the lines of "if you don't get flooded, don't select flood cover". She took this advice and because it hadn't been explained to her, by opting out of the flood cover she had also inadvertently opted out of both storm surge and rainwater run-off cover. She did not know this until she lodged a claim when her home sustained major damage when it was inundated by rainwater run-off following the 2022 Northern Rivers floods as the storm drains near her property failed to manage the high intensity of the heavy rainfall.

We are confident that standardising these natural hazard terms will further reduce some of the problems for consumers. However, it will only partly address the issues. This review should consider other common terms that have proven highly problematic for many years and will continue to be problematic without standardisation. It's our experience that there has been an overreliance on exclusion clauses relating to defects, maintenance, wear and tear, and pre-existing damage/condition. Some of the pain points for consumers include:

- (a) These terms are often broad and general in definition and vary between policies.
- (b) Insurer's own staff interpret these terms differently so there is a lack of uniformity or logic in the application of these exclusion clauses.
- (c) Insurers rely on these exclusion clauses without clearly explaining how and why they apply, providing sufficient evidence, explaining what maintenance is expected and how it could have prevented or mitigated the damage.
- (d) Consumers are unaware or unclear of what is reasonably expected of them to properly maintain their property.
- (e) Consumers often don't have the building expertise or knowledge to identify defects or maintenance needs. In some cases these are hidden behind walls and other building structures and are only identified once exploratory work is done by insurers after a claim is lodged.

Case study – Miriam and Todd Collin's story

The Collin's property in the Riverina was badly damaged in the October 2022 floods. They were isolated for weeks, traumatised and had not been able to make an insurance claim or access any financial support. After being assisted by the DRLS to lodge their claim, they received a decision from their insurer in early 2023 denying the claim based on maintenance issues. There were no details from their insurer about what maintenance they were expected to complete. The DRLS lodged a complaint with the Australian Financial Complaints Authority (AFCA) appealing this decision, arguing the insurer had not provided sufficient evidence to establish the maintenance exclusion

under the policy. In July 2023, the insurer overturned its decision and agreed to accept the insurance claim in full.

5. For those terms that are proposed to be standardised, are there any exclusions that you believe should apply?

LANSW does not propose any specific exclusions to be applied but accept that further consideration as to the scope of each definition will involve decisions around inclusions and exclusions. Our major concern for any exclusion is that they must be defined in plain English terms that can be easily understood by consumers and meet community expectations.

6. Are there any additional natural hazard terms you think should be standardised?

The priority terms that are proposed for standardisation reflects the most recent catastrophes across NSW which is also demonstrated in LANSW's casework. Given the vast scale of flood impacted areas across NSW starting with the catastrophic 2022 floods, we consider all hydrology related terms should be prioritised including storm surge and actions of the sea. While our casework has not necessarily included any storm surge or actions of the sea related matters, we have seen the differing use of these terms by insurers which has only added further confusion for consumers. We are also concerned about the potential risk for future catastrophes such as cyclones, particularly for the coastal regions in NSW that are often impacted by hydrology related extreme weather events. We also see this as an opportunity to avoid the devastation experienced by insureds following the 2010-2011 floods and pre-standardisation of the definition of floods.

Standard cover

7. How well is the current standard cover regime achieving its intended purpose?

LANSW's experience of the current standard cover regime is that it's not achieving its intended purpose. Its purpose was to reduce the complexity of policies so that consumers would have a basic level of cover for what was commonly expected to be covered and in turn consumers would be able to compare the same product across the different insurers.

A critical component of why the regime has been failing is how easy it is for insurers to contract out of the standard cover. Insurers were free to promote policies that offered less than the standard cover so long as they draw the insured's attention to this. To meet this requirement under the *Insurance Contracts Act 1984*, insurers need only to provide a copy of the PDS. We know from all the reports and research (particularly those mentioned in the consultation paper) that consumers have very poor engagement, if any, with their PDS when it comes to making decisions about their policy.

8. Which of the three options for intervention would best achieve the intended purpose?:
Repeal the standard cover regime in its entirety; Amend the standard cover regime to mandate insurers offer a baseline level of coverage for home building insurance only; or

Amend the standard cover regime to mandate a vertically differentiated rating system for home building insurance.

LANSW does not support repealing the standard cover regime in its entirety as the absence of one will not result in better consumer outcomes and certainly would not in any way achieve the intended purpose of why it was introduced. We support amending the standard cover regime to mandate insurers offer a baseline level of coverage for home building and contents insurance. We recognise that a lot of consideration and work will be required to identify an appropriate model for this for it to be effective and successful in achieving the intended purpose of the standard cover regime.

9. Which of the three options is least likely to achieve intended purpose?

Option 1 – repealing the standard cover regime in its entirety.

10. Are there any options to amend standard cover not listed above that you believe should be considered?

No.

11. Should the standard cover regime be retained for insurance products other than home insurance?

Yes. LANSW supports the standard cover regime be retained for all key general insurance products that are already defined under the *Insurance Contract Regulations* including motor vehicle, sickness and accident, consumer credit and travel. We note that home contents insurance doesn't appear to be specifically referred to in the consultation paper, although this may be because it has been grouped together with home building. While many of our clients are homeowners who would likely hold both home building and home contents insurance, there are circumstances where a consumer may hold only one or the other (eg, tenants & landlords) so it's important that home contents is explicitly mentioned as distinct from home building.

We note that most of our insurance casework arising from the various extreme weather event disasters across NSW in the last few years have been about home building and home contents, we also know that our clients experience similar challenges with other general insurance products. We support a reform of the standard cover regime to be applied to all key insurance products as the best chance of achieving the intended purpose for which the regime was introduced to do.

12. Under option 3, on what basis should the various offerings be differentiated?

LANSW does not have a strong view on option 3, but if it is to be considered it would necessarily require research and consumer testing to identify what should be included at each level of cover.



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