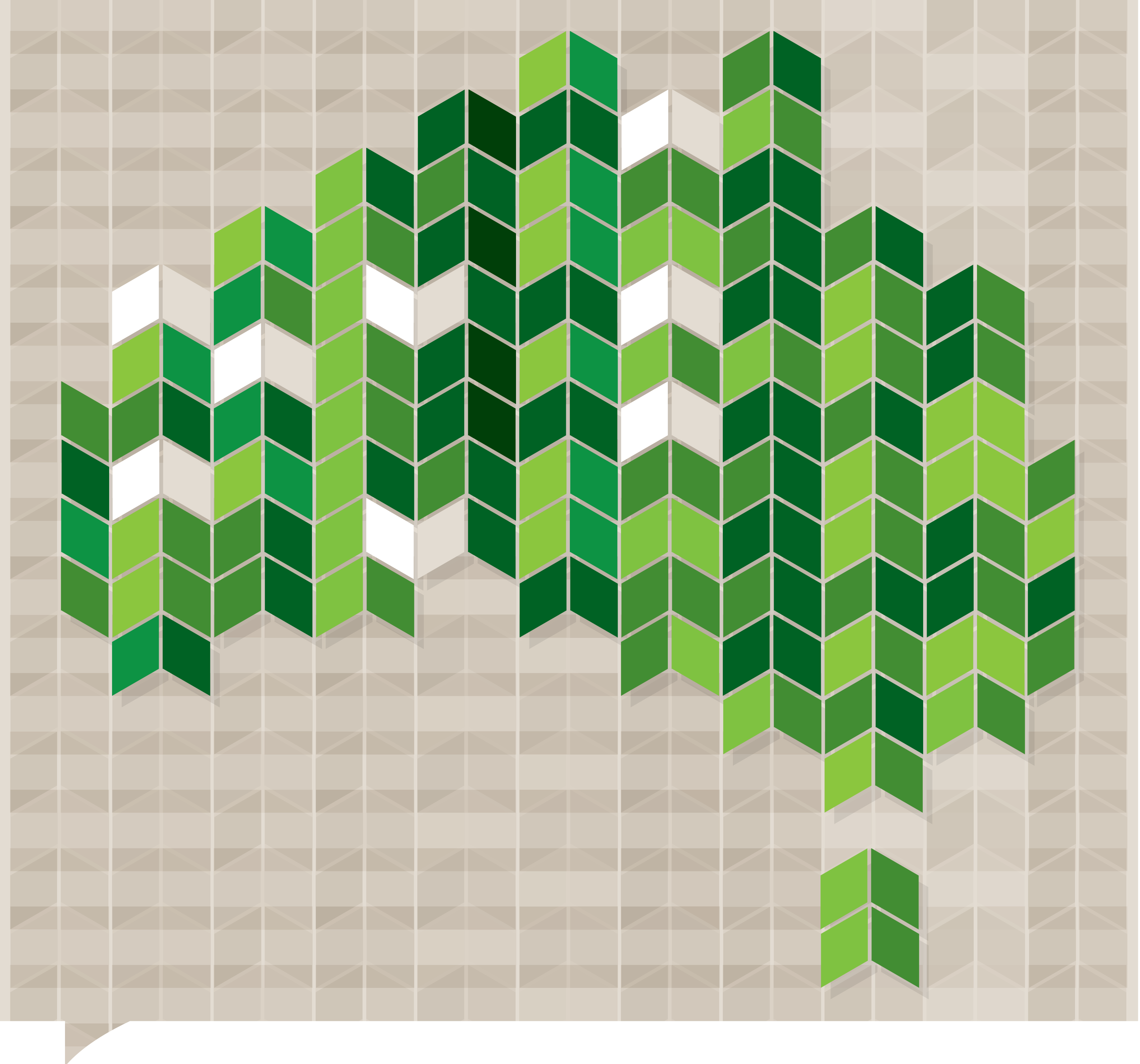

Response to Financial System Inquiry

Final Report

TAL

27 March 2015

Senior Advisor
Financial System and Services Distribution
The Treasury
Langton Crescent
PARKES ACT 2600

Financial System Inquiry – response to consultation

We refer to the recommendations detailed in the Financial System Inquiry Interim Report and make this submission on behalf of TAL Dai-ichi Life Australia Pty Limited (TAL) and its subsidiaries.

As Australia's largest life insurer, providing products and services to consumers directly, through aggregators, financial advisers and within superannuation funds, TAL is well placed to understand first-hand the substantial issues that have been raised as part of the Inquiry, and reflected in the final recommendations. Through its memberships of ASFA and the FSC, TAL has contributed to industry responses.

At TAL, we are very conscious of the important role that life insurance plays in our society. We contribute to and support the lives that people create and the future they imagine. In addition to the submissions made by ASFA and the FSC, we have chosen to call out and specifically comment on our support of the recommendations to:

- Strengthen product issuer and distributor accountability;
- Introduce product intervention powers; and,
- Introduce a mechanism to facilitate the rationalisation of legacy products.

We would welcome an opportunity to discuss this submission with you.

Yours sincerely

Jim Minto
Group CEO and Managing Director

Brett Clark
Deputy Group CEO

TAL Responses

FSI Recommendation 21: Strengthen product issuer and distributor accountability

Introduce a targeted and principles-based product design and distribution obligation.

TAL supports the FSI recommendation to strengthen product issuer and distributor accountability, and believes the proposed legal obligation will help address TAL's concerns about product issuance.

The macroeconomic environment is increasingly complex and volatile. Consumers are becoming more self-directed and want to be more engaged in financial decisions, at a time when their investment and purchasing risks in financial services are greater and will increase.

Against this backdrop is a reduction in the availability of advice. While the use of technology makes product information more accessible, this is not a solution to complexity.

Marketers over many generations have tried to make products and solutions appear more attractive, tending to play down basic risks and encouraging consumer engagement.

It is inevitable that product issuers will continue to develop products and concepts whose introduction can have unintended consequences, while not all consumers are well placed to assess the risks.

Disclosure is not the sole answer to these issues. Longer, more complex disclosure is the enemy of consumer understanding.

TAL believes some simple principles must apply in these circumstances:

- Financial products must, as in other industries, be 'clearly fit for the purpose'.
- Consumers must be able to understand easily who the products are intended for and what they are designed to achieve from a consumer perspective. They must be able to understand in consumer language what 'the purpose of a product is'.
- There must be a basic description of the risks written from a consumer perspective. Consumers must be able to understand what these risks are and how they might impact their transaction and future value from a practical perspective.

A product and distributor obligation would help ensure more appropriate and more consumer-oriented products are manufactured and distributed.

FSI Recommendation 22: Introduce product intervention powers

Introduce a proactive product intervention power that would enhance the regulatory toolkit available where there is risk of significant consumer detriment.

TAL supports the FSI recommendation to provide ASIC with additional product intervention powers as a tool to protect consumers and allow them to have more confidence in the financial services industry.

We support the use of product intervention powers where:

- A product is targeted at a particular segment of the population (or is unsuitable for a segment of the population);
- The population segment identified above is considered vulnerable; and
- The product has features which are unsuitable for this population segment.

TAL supports giving ASIC the ability to issue guidance to the industry as to suitable product features and distribution requirements. We support the power to issue guidance rather than 'black letter' regulation as it provides greater flexibility to respond to changing conditions while still providing consumer protection and transparency.

An example of where product intervention may apply is in relation to stepped funeral insurance premiums, where these are sold to individuals on income-tested government benefits or fixed incomes. A clear body of evidence demonstrates that consumers on fixed incomes are disadvantaged by the stepped premium structure, as prices rise beyond their affordability levels and that these consumers may be better off under a level premium arrangement.

Despite this, yearly renewable (or 'stepped premium') insurance dominates funeral and life insurance in the Australian market for people in these financial circumstances. This type of product is characterised by premiums that increase over time, meaning that while premiums may be low for younger people or those at an earlier stage of the contract duration, they increase significantly over time. At older ages, particularly post-retirement, the increase in the premium year-on-year can become prohibitive when the individual is no longer working and least able to afford the increase.

Market forces do not protect these consumers, and this is a key example of where regulation should be applied to support better consumer outcomes.

TAL Responses (continued)

FSI Recommendation 43: Legacy products

Introduce a mechanism to facilitate the rationalisation of legacy products in the life insurance and managed investments sectors.

TAL strongly supports this recommendation.

It is especially relevant to Life Insurance.

Life Policies are designed, in many cases, to operate for decades and while they are up-to-date at the time of issue, they can become superseded by customer, market and legislative changes over time.

For consumer protection reasons, at present Life Policies can only be changed with the consent of the individual consumer who took out the policy. This effectively a blocks large-scale product rationalisation as all policyholders need to agree to a change for it to deliver required issuer benefits and avoid even more complexity.

Given that old policies must be administered, the costs charged to the consumers holding these products tend to be higher than for new policies, partly reflecting the higher administration complexity when the old products were designed and the different market conditions at that time.

There must be scope to make changes that benefit both consumers and the Life Policy issuer without taking away the consumer right.

TAL has suggested that the Insurance Contracts Act 1984 (Cth) should be amended to allow life companies to unilaterally amend policy terms where it is in the collective interests of policy owners to do so, subject to:

- Receiving independent actuarial and legal advice confirming that this requirement has been met; and
- The insurer having a process in place which allows them to appropriately deal with cases where a policy owner has been materially disadvantaged by a unilateral change to their policy.

TAL is supportive of alternative approaches that achieve the same purpose.

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