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Submission on Consultation Paper – Exposure Draft Insurance Contacts Bill

1 This is a submission by Dentons Kensington Swan on the consultation paper dated 24 February 2022 ('**Consultation Paper**') released by the Ministry of Business, Innovation, and Employment ('**MBIE**') on the Exposure Draft Insurance Contracts Bill.

About Dentons Kensington Swan

2 Dentons Kensington Swan is one of New Zealand's premier law firms with a legal team comprising over 100 lawyers acting on government, commercial, and financial markets projects from our offices in Wellington and Auckland. We are part of Dentons, the world's largest law firm, with more than 12,000 lawyers in over 200 locations.

3 We have extensive experience advising insurers, financial advice providers, and other institutions who will be affected by the proposals set out in the Consultation Paper.

General comments

4 We understand that the regime governing insurance contracts in New Zealand is long overdue for reform. However, this overhaul needs to balance the interests of insurers more readily with those of policyholders. Although insurers may be better resourced than consumer policyholders, and more knowledgeable as to the 'ins and outs' of their specific policies, there is still a place for contracts to be entered into on an open and transparent good faith basis. Without full and accurate information from potential policyholders, insurers will be unable to properly inform themselves of the likely risks involved, potentially undermining the quality of the contract, its fairness for the insurer, and/or the appropriateness of the cover provided.

Summary of our key submission points

5 *Duty of disclosure* - we are concerned that the reframing of the policyholder duty to 'not make a misrepresentation' will result in the creation of lengthy and complex questionnaires for policyholders to fill out prior to entering into any contract of insurance. The resulting increase in costs involved in re-designing and processing applications is likely to be passed through to consumers. It is also likely to add delays and complexity at annual renewal. Requiring insurers to pose extensive and potentially intrusive questions does not lead to a great customer experience, and may result in some applicants deciding not to proceed with seeking the cover they need.

6 *Reasonable care* – it is inappropriate to dictate that omissions cannot constitute a misrepresentation.

7 *Comprehensive approach to insurer's conduct duties* - the implications of the pending reforms under the Financial Markets (Conduct of Institutions) Amendment Bill need to be factored in when imposing any additional duties and possible penalties on insurers, particularly as the duties and conduct obligations broadly align and overlap. There is no need for insurers to be exposed to the potential of 'double jeopardy' as a result of the two sets of reforms.

8 *Prescribed requirements for insurance contracts* - we are uncomfortable with the idea of prescribed requirements for the content, form, and presentation of insurance contracts. Restrictive requirements often result in a bland sameness of documentation, making it more difficult for a policyholder to comprehend the differences between insurers. It also undermines the potential for innovation in the insurance space, and may impose unnecessary cost on insurers through relatively minor differences in the wording and presentation approach they have already implemented.

9 *Proportionate remedies for duty of disclosure breach* - we are supportive of the inclusion of proportionate remedies which reflects current industry practice. Our preference is for the proportionate remedies to be described in such a way that there is flexibility for insurers to use their discretion in applying those remedies.

10 *Client premium* - we would be supportive of moves to align the manner in which intermediaries hold premium money with the client money and client property obligations under the Financial Markets Conduct Act 2013.

11 *Interest payable from 91st day after date of death* – we consider that interest should only be payable from the 91st day after an insurer has been notified of an insured's death. In addition, where payments are to be made to an insured's estate, interest should only be payable from the 91st day after the grant of probate.

12 *Unfair contract terms* - we prefer Option B as this allows the terms of the contract to define the insurance cover. Option A would create an undesirable level of uncertainty.

Specific response to the Consultation Paper

Part 1 – Preliminary provisions

Question 1 – Do you have any feedback on Part 1 of the Bill?

Nothing to submit.

Part 2 – Disclosure duties and duty of utmost good faith

Duty for consumers / Group Insurance

Question 2 - Do you have any feedback on the Bill's provisions in relation to the duty for consumers to take reasonable care not to make a misrepresentation, including the matters that may be taken into account to determine whether a consumer policyholder has taken reasonable care not to make a misrepresentation?

The framing of the duty for consumer policyholders 'not to make a misrepresentation' shifts the onus onto insurers to ask the right questions at the time a policy is entered into. This tilting of obligations raises a number of concerns. A key issue likely to arise from this new duty is the creation of lengthy and complex

questionnaires by insurers to cover all potential risks. Such questionnaires and related policy documents are unlikely to be in the best interests of policyholders, whilst also conflicting with the new regime's focus on clear and concise documents.

In addition, the costs associated with drafting a comprehensive framework of questions and processing the responses are likely to be passed on to consumers. Placing barriers to taking out insurance, such as those created by lengthy and sometimes intrusive questions, may also deter some from proceeding, which is not a good customer outcome.

In order to minimise the increased risk to insurers, and without getting too bogged down in prescribed wording, a standardised framework of questions could be developed for the various policy types as guides to assist insurers to comply with the new regime – particularly if 'open-ended' questions are no longer an option. With insurers taking on increased risk under the new regime, it is desirable to minimise compliance difficulties and costs.

The requirements under Part 2 of the Bill also broadly overlap with fair conduct principles being introduced under the Financial Markets (Conduct of Institutions) Amendment Bill. Insurers will have dual obligations to put policyholders first and treat them with care. Conduct obligations for insurers must factor in the requirements imposed under the Insurance Contracts Bill, or vice versa, otherwise insurers face the possibility of regulatory action on two fronts for the same conduct (unlike banks and non-bank deposit takers).

Finally, we believe the concept of reasonable care, as currently articulated in the draft Bill, is too wide. As drafted, failure to answer or fully complete a question is taken not to be a misrepresentation. Ordinarily such actions are able to be viewed as a misrepresentation by omission. There needs to be some responsibility placed on policyholders, and a requirement for them to take reasonable steps to seek assistance if they have doubts about what a question is asking. This could simply involve discussing the question with their intermediary or direct with the insurer to understand what information is being sought via the insurer's question. Clause 17 could include consideration of the extent to which the policyholder proactively sought further information or help.

We believe clause 16 and 17 should be removed and included under clause 15 as matters to be 'taken into account' as a whole, rather than standalone considerations. If clause 17 remains as is, then the entire onus of the reworked duties falls on insurers. This is inequitable, and risks unintended consequences arising from how insurers will need to respond to this added risk. We understand there is a need to factor in the asymmetry of expertise as between insurers and policyholders, however, at present Part 2 undermines the concept of utmost good faith operating on both sides.

Remedies for breach of consumer duty

Question 3 - Do you have any feedback on the Bill's provisions in relation to remedies for breach of the consumer duty?

We support the inclusion of proportionate remedies for breaches of the consumer duty. This is the practice adopted by most insurers now to ensure the best outcome for both parties.

The remedies as framed in the tables in the consultation document (pages 14 and 15) appear narrower than as drafted in Schedule 2 of the Bill. Schedule 2 provides that insurers 'may' avoid the contract or take other actions depending on the type of misrepresentation. We submit that the remedies in the Bill be framed as 'flexible remedies' for insurers, with Schedule 2 acting as a guideline. Insurers currently have broad discretion to address misrepresentations with outcomes in the best interest of policyholders. It would be a shame if the Bill overly constrained the remedies available, particularly for insurers who work with

policyholders to resolve matters in a mutually beneficial manner.

Question 4 - Do you have any feedback on the Bill's provisions on remedies for breach of the consumer duty in relation to life insurance policies where the misrepresentation was not fraudulent and more than three years ago?

Nothing to submit.

Duty for non-consumer insurance contracts

Question 5 – Do you have any feedback on the Bill's provisions in relation to the disclosure duty for non-consumers?

Nothing to submit.

Remedies for breach of duty of fair presentation

Question 6 – Do you have any feedback on the Bill's provisions in relation to remedies for breach of the non-consumer duty?

We support the inclusion of proportionate remedies for breaches of the non-consumer duty (along the same lines as discussed above in response to Question 3).

Insurer's duties

Question 7 - Do you have any feedback on the provisions in relation to the insurer's duties to inform policyholders of the disclosure duties, and insurer access to third party information, including how the duties apply for variations of insurance contracts?

Although we are reluctant to see an overly prescriptive regime put in place, one area where we do consider some 'recommended wording' would be useful is to set out how insurers can describe the policyholder's duty and the consequences of failing to comply with that duty. Recommended wording in this area could take the form of standardised safe harbour wording, whereby insurers can either adopt the suggested form or develop their own descriptions of the duty at their own risk.

The fact all insurers will have the same duty means providing recommended wording in the statute works to reduce unnecessary risks (and therefore costs) for insurers. Failure to inform policyholders of their duties will result in insurers losing access to proportionate remedies along with facing the possibility of regulatory sanctions under Part 6 of the Financial Markets Conduct Act 2013, such as censure or even licence suspension or cancellation, for breach of a market services licensee obligation. Setting out standardised wording would ensure the duty is explained in a consistent manner across insurers and insurance types, whilst removing doubt as to whether a proportionate remedy is available to the insurer.

Question 8 - Do you have any feedback on the consequences in the Bill if an insurer breaches duties to inform policyholders of the disclosure duties, and insurer access to third party information?

As discussed above, the consequences of a breach are severe given the risk can readily be removed via provision of suggested 'safe harbour' wording. Ideally, if an insurer uses safe harbour wording then clause 58 would not apply in respect of the duty to inform. Regardless, the proposed consequence appears disproportionate, with greater flexibility required to factor in the seriousness of any failure.

Duty of utmost good faith

Question 9 - Do you have any feedback on how the Bill codifies the duty of utmost good faith?

We are uncomfortable with the codification of the existing common law duty of utmost good faith as currently proposed. An insurer must still act in good faith, yet a consumer policyholder only needs to take reasonable care not to make a misrepresentation. Conceptually the duty of good faith functions to ensure that insurers are told all they need to know to make an accurate assessment of the risk when formulating the terms of, and entering into, a contract of insurance with a policyholder. The duty negates the asymmetry of information that ordinarily favours policyholders.

In practice, the Bill undermines the duty of utmost good faith and unduly tilts the balance toward policyholders codifying the asymmetry of information by allowing policyholders to withhold information by virtue of failing to answer questions or providing incomplete information. In such circumstances the burden again falls on insurers to do the additional work in seeking further information from policyholders, and risks unintended negative consequences for consumers in the form of increased cost and restrictions on cover availability.

Specified intermediaries passing on information

Question 10 - Do you have any feedback on the Bill's provisions relating to information provided by a policyholder to a specified intermediary?

The requirement for specified intermediaries to pass on information to insurers makes practical sense. However, we have reservations about specified intermediaries making their own determinations as to what is material and what is or may be a misrepresentation. The onus on the intermediary to determine such matters places them in a tricky position regarding the interests of their clients. And it is likely intermediaries will adopt different interpretations as to what is or is not material.

We consider insurers are best placed to consistently assess the relevance and materiality of any information provided by policyholders. Perhaps the provisions are best drafted to allow for specified intermediaries to pass on all information, and to highlight information they believe may be material or a misrepresentation. The drafting should provide that the passing on of information by a specified intermediary to an insurer is in the best interest of policyholders, i.e. it assists policyholders not to make misrepresentations and ensures the insurer is fully informed so the policy can provide proper cover. This is of particular relevance where specified intermediaries are also captured by the advice duties of the Financial Markets Conduct Act 2013 including to give priority to client interests.

Question 11 - Do you have any other feedback on the drafting of Part 2 of the Bill?

Nothing to submit.

Part 3 – Terms of insurance contracts

Time limits for making claims under claims-made liability policies

Question 12 - For claims-made policies, do you consider that 60 days after the end of the policy term is an appropriate period for allowing the policyholder to notify relevant claims or circumstances that might give rise to a claim?

Nothing to submit.

Question 13 - Do you consider that insurers should be required to notify policyholders in writing no later than 14 days after the end of the policy term of the effect of failing to notify a claim or circumstances that might give rise to a claim before the end of the 60 day period?

Nothing to submit.

Question 14 - Do you have any other comments on clause 69 of the Bill (Time limits for making claims under claims-made liability policies)?

Nothing to submit.

Insurers' ability to rely on increased risk exclusions

Question 15 - Do you have any feedback on the exclusions listed in clause 71(3), which are not subject to the rule for increased risk exclusions in clause 71(1)?

Nothing to submit.

Third party claims for liability insurance money

Question 16 - Do you have any other feedback on Subpart 4 of Part 3 of the Bill (Third party claims for liability insurance money)?

Nothing to submit.

Question 17 - Do you have any feedback on Schedule 3 of the Bill (Information and disclosure for third party claimants)?

Nothing to submit.

Carrying over and updating existing provisions

Question 18 - Do you have any comments on not carrying over section 10(1) of the ILRA 1977?

Nothing to submit.

Question 19 - Do you have any other feedback on the drafting in Part 3 of the Bill?

Nothing to submit.

Part 4 – Payment of monies to insurance intermediaries

Feedback sought in relation to holding of premium money

Question 20 - Do you consider that changes should be made to requirements for how insurance brokers must hold premium money such as restrictions on brokers' ability to invest or more stringent requirements in line with the client money and property rules in the FMC Act?

The reforms to the existing law regarding payments of monies to insurance intermediaries are largely superficial. We think there is an opportunity under the Bill to streamline matters so that intermediaries dealing with client money are brought under the 'client money and client property' requirements contained in the Financial Markets Conduct Act 2013. This removes the risk of inconsistent practices and conflicting regulatory obligations, especially where many intermediaries operate in more than just the insurance space.

Proposed penalties for non-compliance

Question 21 - Do you have any feedback on the proposed penalties for non-compliance with Part 4 of the Bill?

Nothing to submit.

Question 22 - Is it necessary to retain clause 102 (broker to notify insurer within 7 days if a premium has not been received by the broker), and if so, what should be the consequence for breach of clause 102?

Nothing to submit.

Question 23 - Do you have any other feedback on Part 4 of the Bill?

We understand the difficulty in attempting to use specific descriptions across the various pieces of legislation, however, there is a proliferation of terms in the Bill ('insurance intermediary', 'specified intermediary', and 'broker'). When placed alongside the Financial Markets (Conduct of Institutions) Amendment Bill and existing everyday use of the terms, as well as the established concept of agency, it is important to achieve as much consistency in use of terms as possible. We suggest it is timely to take this opportunity to align at least some of the terms and obligations across the board. Such alignment should also take into account changes made regarding the provision of insurance advice under the Financial Services Legislation Amendment Act.

Part 5 - Contracts of life insurance

Interest payable from 91st day after date of death

Question 24 - If you consider that change needs to be made regarding interest payable from 91st day after date of death, please provide any further reasons and provide feedback on whether interest should only begin accruing after 90 days if the insurer has been notified of the death claim and (where relevant) letters of administration or probate have been obtained.

We submit that interest should only be payable from the 91st day after an insurer has been notified of an insured's death. In addition, where payments are to be made to an insured's estate, interest should only be payable from the 91st day after the grant of probate. While we acknowledge that the intention of the provision is to incentivise insurers to deal with claims in an efficient and timely manner, certain circumstances, not least of all the application for probate, will be outside of the insurer's control, meaning the provision will not have the desired incentive effect.

Additionally, while it is a good policy objective to ensure that the recipient does not miss out on interest that they could have been accruing but for the delay, where there is a no-fault delay it would not be sound in principle to penalise the insurer. Calculating the 90-day period from the date of notification of death or grant of probate goes some way to addressing this issue by removing a significant factor outside of the control of the insurer.

Mortgaging of policies

Question 25 - Do you have any feedback on the proposal that any mortgaging of life insurance policies under new policies be dealt with under the Personal Property and Securities Act 2009?

Nothing to submit.

Assignment of policies

Question 26 - Do you have any feedback on the Bill's requirements relating to assignments and registrations generally?

Nothing to submit.

Surrender value / Minors / Life insurance for spouses, partners and children / Other provisions

Question 27 - Are section 75A of the LIA (relating to a policy entered into by a person for the benefit of the person's spouse, partner or children) or section 2(1) of the Life Insurance Amendment Act 1920 (relating to the reversion or vesting of life policy assigned to a spouse or partner) still necessary?

Nothing to submit.

Question 28 - Do you have any other feedback on Part 5 of the Bill?

Nothing to submit.

Part 6 – Regulation-making powers and miscellaneous provisions

Question 29 - Do you have any feedback on Part 6 of the Bill?

Nothing to submit.

Part 7 – Unfair contract terms and presentation of consumer policies

Marie Insurance Act 1908

Question 30 - Do you see any unintended consequences from removing these provisions from the MIA?

Nothing to submit.

Unfair contract terms

Question 31 – In relation to unfair contract terms: which option do you prefer and why?

We strongly prefer Option B. Option A would create an undesirable level of uncertainty. Such uncertainty for insurers and underwriters would likely result in increased premiums or limits to the amount of cover insurers are willing to provide.

Option B allows the terms of the contract to define the insurance cover. Retaining a broader list of exceptions preserves the ability for insurers to develop policies, provide cover as they see fit, and adjust premiums accordingly. Ideally, the list of exceptions would also include the payment of premiums under Option B or expressly clarify that the premium payable is excepted as part of the 'upfront price payable' under the contract.

Question 32 - Do you have any feedback on the drafting of either of the options?

As noted above, we consider that the list of exceptions under option B should, for clarity, expressly include the payment of premiums.

Duties to assist policyholders to understand insurance contracts / Obligations for contract wording and presentation

Question 33 - Do you have any comments on the obligation that consumer insurance contracts be worded and presented in a clear, concise and effective manner?

There is benefit in ensuring contractual terms are clear, concise, and effective. However, care must be taken to ensure that a balance is struck between plain wording and the need for technical specificity in insurance contracts. In many cases the technical word is the right one to use because it is either a medical term, there is extensive case law behind the meaning and interpretation, or it aligns with underlying reinsurance treaties.

Regulations relating to form and presentation of contract / Regulations relating to publishing information

Question 34 - Do you have any comments on the regulation-making powers in clause 184?

Nothing to submit.

Question 35 - Do you think regulations specifying form and presentation requirements for consumer, life and health insurance contracts (e.g. a statement on the front page that refers to where policy exclusions can be found) would be helpful? If so, please explain.

Given our experience with product disclosure statements under the Financial Markets Conduct Act 2013, we have concerns about any overly prescriptive and restrictive regulations with respect to the form and presentation of consumer, life, and health insurance contracts.

Many insurers have worked or are working on 'plain-Englishing' existing and new insurance policies. It would be an unfortunate consequence if insurers, as a result of these reforms, had to yet again go through the costly and time-consuming exercise of revisiting documentation and policies to align with anything more than a high-level drafting principle. Any move toward prescription must be carefully considered as it would also hinder an insurer's ability to develop and explain the terms of bespoke and innovative products.

Question 36 - Do you think regulations specifying publication requirements for insurers would help consumers to make decisions about insurance products? If so, please explain.

Although averse to prescription, we consider that there is merit in prescribing a description of the policyholder's duty of disclosure. Similar to our comments under question 7 above, we are of the view that any prescription should be in the form of a safe harbour to ensure a satisfactory cost and benefit ratio for both insurers and consumers. Further, any publication requirements about insurance products should also consider how such information would be presented across all mediums including social media platforms.

Timing and transitional arrangements

Commencement

Question 37 - Do you have any initial feedback on when the Bill's provisions should come into effect?

Related to question 38 below, we propose that the Bill allow a minimum 2-year transition period once all relevant law (Act and any regulations is final) for the Bill's key provisions (in particular Part 2) to take full effect. This provides insurers with time to plan for transition, update documentation or, in some cases, develop new documentation, and put in place new systems and processes to effectively and efficiently comply with their duties under the new regime.

Transitional arrangements

Question 38 - Do you have any feedback on the transitional provisions in Schedules 1 or 4, or other proposed transitional arrangements?

As each renewal creates a new contract of insurance for general policies, and with most of those policies on one-year terms, the transitional arrangements in clause 2 of Schedule 1 potentially create a considerable amount of work for insurers to do in a short timeframe at transition (within a year or so of the new duties coming into force).

There does need to be a definite deadline for the new duties becoming effective, however a longer transitional phase could be instituted. Given the large-scale changes to the disclosure duties we anticipate prudent insurers will undertake a review of their renewal processes with the view toward asking more questions at renewal time. With this in mind insurers could be allowed to select an 'effective date', perhaps within a two-year transition period between, to comply with the new regime. (The new regime would apply to an insurer from the earlier of their elected 'effective date' or the 'drop dead' date when the new regime is fully in force.)

Schedules 5 – Amendments to other Acts

Question 39 - Do you have any feedback on Schedule 5 of the Bill?

Nothing to submit.

Further information

13 We are happy to discuss any aspect of our feedback on the Consultation Paper.

14 Thank you for the opportunity to submit.

Yours faithfully

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