ICNZ Insurance Council of New Zealand

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Responsible Lending Code
Competition and Consumer Policy Team
Ministry of Business, Innovation and Employment
PO Box 3705
Wellington 6140

By email: consumer@mbie.govt.nz

To Whom It May Concern,

Submission on Draft Responsible Lending Code

1. Thank you for the opportunity to comment on MBIE's Draft Responsible Lending Code ('the draft code'). We provide this submission on behalf of the Members of the Insurance Council of New Zealand ('ICNZ').

2. Broadly speaking, we support the draft code. However, there is one major area of concern for our Members in section 9 of the draft code. We strongly submit that lenders should not be required to communicate 'key exclusions' to borrowers.[1] It is not possible to identify 'key' exclusions, and doing so would mislead and disempower consumers. Our full reasons are below. We also make two minor submissions that:
    - paragraphs 9.2.e. and 9.5 should only apply to consumer credit insurance, and
    - paragraph 9.17 should specifically accommodate any cooling-off period in the insurance contract.

3. Please feel free to contact our legal counsel Nick Mereu by email nick@icnz.org.nz or phone (04) 495 8008 if you have any questions or require further information.

[1] Under paragraph 9.10.d. of the draft code.

About ICNZ

4. ICNZ is the industry representative for fire and general insurers in New Zealand. We aim to assist our members in the key areas that affect their business through effective advocacy and communication.

5. ICNZ currently has 29 members who collectively write more than 95 percent of all fire and general insurance in New Zealand. ICNZ members, both insurers and reinsurers, make up a significant part of the New Zealand financial services system. ICNZ members currently protect more than half a trillion dollars' worth of New Zealanders' assets.

6. ICNZ plays an active role in representing the insurance industry. Our members are licensed under the *Insurance (Prudential Supervision) Act 2010* and are signatories to the Fair Insurance Code, which requires our members to act according to industry best practice standards. We also perform an important role in informing and educating consumers about key insurance issues and risks.

Consumer credit insurance and asset insurance are distinct insurance products

7. We would like to reiterate a point we made in our submission of 15 August 2014. The draft code applies to both asset insurance and consumer credit insurance, but these are very different types of insurance product.

8. Asset insurance protects an asset, or assets. For example, house and contents insurance protects your home and personal property. Consumer credit insurance, on the other hand, protects the borrower's ability to repay a debt. If you have a home loan and consumer credit insurance, and you become unemployed, then your consumer credit insurance will continue to pay your home loan payments to the lender.

9. We submit the responsible lending code must account for the differences between these types of product. We recognise the distinctions made in paragraph 9.2 of the draft code and thank MBIE for its consideration of our submission. However, as noted below, there are other areas where the distinction must, in our view, be made clearer.

We support highlighting key features of insurance

10. We note the lender's overarching obligation in paragraph 9.10 is to **clearly highlight** the key features of the credit-related insurance contract in a way that **draws the borrower's attention to that information** at a time that assists the borrower to make an informed decision. We support this overarching obligation. Clearly highlighting key information in a way that draws the borrower's attention to it will assist borrowers to make informed decisions without requiring lenders to give borrowers financial advice.

11. We also support five of the six key features listed at paragraphs 9.10.a.-f. We do not support subparagraph d in its current form, and we submit that it should be amended by deleting the word 'key'. In the first instance we are unsure what the word 'key' refers to.

What exclusions are 'key'?

12. In our view, 'key' exclusions could mean either:
    - generic policy limits to the cover available, or
    - fact-specific or circumstance-based exclusions.

13. Generic policy limits outline the boundaries of the risk insured and **apply to all risks insured**, regardless of the particular claim the insured person may eventually make. These limits include the monetary limits of cover provided for each benefit of the policy (for example, the maximum sum insured) and any applicable excesses. It is relative simple to identify these limits and draw the insured borrowers' attention to them before entering into the insurance contract. Paragraphs 9.10.c. and 9.10.e. already identify all of the limits that are appropriate for credit-related insurance, though we would add 'any applicable excess' to this list of limits.

14. Fact-specific exclusions carve out **particular** risks that are unacceptable to the insurer. They tend to be based on circumstances particular to an insured that has suffered a loss. For example:
    - Payment protection insurance policies tend to exclude losses caused by criminal acts and alcoholism by the insured.
    - (Asset insurance policies such as) motor vehicle insurance policies tend to exclude losses caused by driving while over the blood alcohol limit.

    It is not possible to identify which of these exclusions will be relevant to a particular insured borrower before the insured event happens, much less before the insurance contract is entered into.

15. If the draft code is meant to mean 'generic policy limits' when it refers to 'key exclusions', then we submit a new subparagraph should be inserted with a reference to 'any applicable excess payable by the insured'. We note that excesses may already be captured by paragraph 9.10.c.

16. Either way, we submit the word 'key' must be deleted from paragraph 9.10.d. 'Key' exclusions suggests that there may be some exclusions that are more pertinent to an insured than others. This is patently untrue. Every policy term forms part of the contract of insurance. Each term has equal importance. Exclusions, in particular, can only become 'more important' than other exclusions or 'key' after the fact – that is, after the insured has suffered a loss.

We do not support identifying 'key' exclusions

17. At present, the draft code appears to require lenders to draw specific exclusions to the borrower's attention. Our objections to identifying key exclusions instead of all exclusions are:
    - It will mislead and disempower borrowers. All terms written into the policy wording are relevant. Drawing a borrower's attention to a select few terms before the contract runs the risk that the borrower will only pay attention to those terms at the expense of understanding the whole insurance contract. Only by reading the contract as a whole can borrowers become fully informed as to whether the insurance meets their requirements and objectives.
    - It runs contrary to current insurance contract law. An insured is obliged at law to read the policy wording. This obligation applies to every contract of insurance, both at common law and under the specific terms of insurance contracts. If such a fundamental change were to be made to any category of insurance contract, we would expect it to be discussed as part of a full and separate review of insurance contracts law, not as part of a non-binding non-legislative instrument following credit law reform.
    - It goes much further than the responsible lender principles in the Act. The best way to assist borrowers to make informed decisions about insurance contracts is to:
        1. clearly highlight that there are limits to cover
        2. draw attention to where the borrower can read about those limits, and
        3. to provide contact details for an appropriate person for the borrower to speak to if they have any further questions (either by referring the borrower to the insurer directly or to obtain independent financial advice).
    - It runs the risk of giving 'financial advice' to the borrower. Drawing attention to particular exclusions, applicable to the borrower's particular circumstances inappropriately crosses the line into financial advice. We also submit that lenders should not be forced to give financial advice through subordinate regulation.

18. For clarity, we do support a requirement for the lender to draw the borrower's attention to the section or pages of the policy wording that contain the full list of exclusions from cover. We also support a requirement for the lender to draw the borrower's attention to any applicable conditions. Conditions of the insurance contract are equally important for an insured that wishes to make a claim. For example, many insurance policies limit the amount of time an insured has to make a claim under the policy. If an insured's delay in notifying the insurer prejudices the insurer, then the insurer may decline the claim.

19. Finally, MBIE may also wish to consider how a requirement to draw the borrower's attention to 'key' exclusions applies to asset insurance and consumer credit insurance as distinct types of insurance product. Some of our Members' consumer credit policies are a

few pages long and only contain a half dozen or so exclusions. Other Members' asset insurance policies can be 20 or more pages long with 20 or more exclusions. Our position is that the requirement is inappropriate for any type of insurance policy.

Paragraphs 9.2.e. and 9.5 should only apply to consumer credit insurance

20. As currently drafted, paragraph 9.5 applies to 'any cover'. We submit that paragraph 9.5 is not relevant to asset insurance, and should be amended by deleting the words 'any cover' and replacing those words with 'consumer credit insurance'.

21. Take, for example, a borrower who needs bridging finance of $1,000 to help fund a $5,000 car purchase. The borrower also wants asset insurance to cover the car. The lender offers credit at, say, $1,000 on a three month term with interest payable at 30 percent per annum. The lender also offers a comprehensive motor vehicle insurance policy (asset insurance) underwritten by a third party insurer, which will insure the car at market value for up to $5,000. The premium for this insurance is $1,000 for a one year period. In this instance, the credit is a 'high-cost short-term credit agreement'. The asset insurance is 'credit related insurance' and subject to the draft code.

22. Our concerns with paragraph 9.5 are twofold. First, the value of cover is said to be relative to 'the cost of the premium'. This assumes that the insurance offering is not worth the premium quoted for it. The level of premium for any insurance product reflects the risks that an insurer accepts on behalf of an insured to indemnify the insured. The cost of premium by itself does not in any way diminish how valuable the cover provided may be for any particular insured.

23. We understand that the key relationship MBIE seeks to regulate is either:
    - how the cost of premium relates to the cost of credit, or
    - how the value of cover relates to the cost of credit.

    If our understanding is accurate, we submit that an amendment should be made to paragraph 9.5 accordingly.

24. Second, the policy intent underlying paragraph 9.5 appears to relate to consumer credit insurance, not to asset insurance. Paragraph 9.5 assumes that the value of 'any cover' is likely to be low in the context of high-cost short-term credit, but the value of asset insurance relates to the asset, not the credit used to facilitate the purchase of the asset, and so bears no relationship to the nature of the credit agreement.

25. We submit that paragraph 9.5 should be revised to apply to consumer credit insurance only.

26. Paragraph 9.2.e. also assumes that comparing premium with the amount of credit advanced is appropriate. We submit the comparison is not appropriate for asset

insurance. On the above example, the level of premium is high compared to the amount of credit advanced, but that in no way diminishes the value of the insurance product. For asset insurance, the value of the insurance product is related to the insured asset, not to the credit financing the asset.

27. We submit that asset insurance should not be subject to paragraph 9.2.e.

Paragraph 9.17 should specifically refer to cooling-off periods

28. In our view, the reference to 'sufficient opportunity' in paragraph 9.17 is too vague. We submit paragraph 9.17 should be amended to specifically allow cooling-off periods in insurance contracts to be considered as a 'sufficient opportunity'.

29. We understand the 'sufficient opportunity' wording reflects the lender's obligation for credit agreements in paragraphs 7.12-7.15 of the code. Paragraph 7.12.a. allows the borrower to take information off-site, away from point-of-sale, to consider offers of credit (and insurance through paragraph 9.17). However, because of the opening wording of paragraph 7.2, we understand this requirement must be satisfied **before** the borrower enters into the contract. We submit that this requirement is inappropriate for insurance contracts.

30. Insurance policies have cooling-off periods which give the insured the opportunity to cancel within a certain period (usually up to 30 days), without penalty. They allow the insured to consider the full insuring terms away from point-of-sale environment. This allows far more time for the borrower to read and understand the terms of the policy, seek advice, and shop around for other insurance if the lender's insurance is not suitable for the borrower's needs. In our view, it is difficult for a borrower to dispassionately process the amount of information that needs to be processed at point of sale, especially for an insurance contract that is contingent on a credit contract, which itself is contingent on the sale of the good or service originally sought out by the insured.

31. We would also add that insureds can also cancel their policies at any stage and not be obliged to continue paying premium. If the insured has paid premium in advance, they will be entitled to a pro-rata refund of overpaid premium (subject to any claims the insured may have made). These features distinguish insurance contracts from credit contracts.

32. We submit that paragraph 9.17.a. should specifically refer to cooling-off periods by adding the words '…, either before the relevant insurance contract is agreed to, or through a sufficient cooling-off period in the insurance contract…' at the end of the paragraph. Combined with paragraph 9.10.f. of the draft code, borrowers will be able to take the time to fully read and understand the insurance contract and make any appropriate inquiries

without penalty if they ultimately decide the insurance contract is not appropriate for their needs.

In closing

33. Thank you for your time and the opportunity to submit. Please feel free to contact our legal counsel Nick Mereu by email nick@icnz.org.nz or phone (04) 495 8008 if you have any questions or require further information.

Yours sincerely,

Nick Mereu
Legal Counsel