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INSURANCE PRODUCT REPLACEMENT ADVICE – A CASE IN POINT

Trevor Harris

This court case is something all risk writers and financial planners should acquaint themselves with. The human story behind the case also appeared on the ABC program 'Four Corners' on 5th May 2014 in a joint investigation with Fairfax Media.

The client

Noel Stevens was a long-standing customer of Commonwealth Bank (CBA). He was a 49 year old divorcee with limited education and extremely modest financial means. At the age of 16 years he started work as a builder's labourer, and later became a dogman (tower-crane loader), rigger and scaffolder.

In September 2010, Mr Stevens received an unsolicited phone call from a bank teller or customer support officer from his local CBA branch in Melbourne, in order to discuss his 'banking situation' with the bank. In all likelihood he was being targeted for financial product sales. CBA knew he had a life insurance policy with Westpac from his banking transaction records. He was not much good to them as a banking customer as he had very limited savings and no loans. Stevens subsequently met with a CBA financial planner at the bank, by referral from the bank's customer support officer.

In the course of the meeting, the planner scoped out the area of advice to insurance only advice, and indicated to Stevens that CBA had a suitable substitute product to the Westpac life insurance policy he currently held, which he ought to consider. It was suggested to Stevens that it would be better for him to have all his financial arrangements with the one bank. Stevens gave evidence that the planner had represented to him that he could do a 'better deal' on the insurance policy than his existing Westpac policy. Stevens had a Westpac term life policy for a sum insured of $298,000 which he had had for seven years. CommInsure could offer the same sum insured for a term life policy, but with a trauma benefit as well, all at an equivalent or marginally cheaper first year premium than his existing Westpac policy.

On this basis, Stevens agreed to the preparation of a statement of advice (SOA). The advice document was presented to Stevens at a subsequent meeting in October 2010, which recommended he apply for a CommInsure term life and trauma policy for the same sum insured as his existing Westpac term life policy, and subsequently cancel his existing policy. Stevens proceeded with the advice as documented in the SOA. The insurance application process was undertaken in that same meeting via a computer-based insurance proposal system which then accepted that proposal without any need for underwriting assessment. Stevens presented as a 'clean skin', essentially. The computer-based proposal system accepted the proposal on the spot, and the planner informed Stevens his proposal for life insurance had been successfully processed and had been unconditionally accepted by CommInsure through that system. Mr Stevens then proceeded to cancel his existing Westpac life insurance policy.

The claim

Not 12 months later, in September 2011 tragically Stevens was subsequently diagnosed with terminal pancreatic cancer and given six months to live. He lodged his claim with CommInsure in November 2011. On 23 December 2011, CommInsure declined his claim as a result of alleged material non-disclosure. In late April 2012, legal proceedings were initiated by Stevens' lawyer against CommInsure and Commonwealth Financial Planning. The proceedings were expedited by the judge due to the rapidly diminishing health of Mr Stevens.

Stevens' actual medical history

Stevens may have presented as a clean skin in his CommInsure insurance proposal, however his medical records told a different story.

- He had received counseling in 2008 to assist him in quitting heavy smoking.
- He had a history of heavy drinking episodes prior to 2010. Stevens told his doctor in 2010 that on occasions he would drink 10 stubbies of beer a night. He had been counseled for heavy alcohol consumption.
- Financial records during 2010 showed heavy expenditure at local bottle shops. His young daughter swore an affidavit that she at times used her father's credit card to buy alcohol for her own use and her friends. The judge found this evidence credible.
- He had a history of raised liver function test results, raised cholesterol, and episodes of recurrent gastric reflux.
- Medical records also revealed past episodes of coughing up blood and black phlegm.
- Stevens had also been diagnosed with Hepatitis C, 20 years earlier.

Problems with the advice process and implementation

The judge found that the initial meeting and discussion initiated by the financial planner did not canvass with Stevens the need for him to consider possible changes in his health since he had effected the 2003 policy with Westpac, where if such changes were relevantly present, these might affect his insurability.

Stevens claimed that during the meeting in which the SOA was presented and the online insurance proposal completed and submitted, he was simply asked to sign the paperwork as authorisation to go ahead, but was not asked or advised to read the SOA or CommInsure Product Disclosure Statement. He also denied being asked detailed questions about his health status (except during the online insurance application process).

The judge found that the CBA financial planner failed to adequately inform Stevens of the consequences of potential material non-disclosure of health and related matters. He also found that the planner's assertion to Stevens that the CommInsure policy would be 'a better deal' for him and that it represented a like-for-like policy were both misleading and deceptive representations insofar as any innocent material non-disclosure by Stevens would allow CommInsure to avoid the policy within the first three years, under section 29 of the Insurance Contracts Act 1984.

In some sessions of the hearings (held at Stevens' home) the comprehensiveness of the defendants' cross examination of Stevens was watered down in light of the fact that he was on intravenous morphine for pain relief at the time and was tired, confused, 'spinning out' and only months from death. This was agreed on and accepted by both parties. This made it difficult for the defendants in that they were relying on the proposition that Mr Stevens had given evidence that was unreliable and should not be accepted.

An insurance underwriter gave evidence to the court that the proposal by Stevens for life insurance would not have been accepted if the facts within the medical records had been disclosed and CommInsure would not have underwritten the risk or offered him a policy of life and trauma insurance. The underwriter indicated that, had Stevens answered the computer-based underwriting questions correctly, it would have automatically triggered additional and more comprehensive follow-up questions to be answered, and would have prompted the insurer to seek a medical questionnaire from his general practitioner, and perhaps even prompted a medical assessment to be performed.

The judge's view was that Stevens' non-disclosure in the insurance proposal occurred innocently, and was a function of the online nature of the application process. Stevens was not given the opportunity to fully consider and review his answers before they were electronically submitted to the insurer.

"These events have arisen because the CML [CommInsure] proposal was prepared under the computerised "Write-Away" system, where the important foundation form was not printed off for Mr Stevens to check before it was submitted to the insurer for automated acceptance. It was an important document, which, if filled out incorrectly, or with insufficient detail or disclosure, as I have found occurred in this case, the ramifications for the proponent would be potentially and foreseeably financially disastrous. This was the effect in this case because the transaction proceeded in haste, on-line, without Mr Stevens being orally advised of the need to ensure factual accuracy and where ordinary prudence suggested that the form be given careful consideration including by checking details of disclosure against factual and medical records." (Levy, SC, District Court Judge)

The quote

The planner had represented to him that he could do a 'better deal' on the insurance policy than his existing Westpac policy.

The quote

Premium comparisons and quotation estimates represent best case scenarios of insurance pricing for a client.

And further:
"In the circumstances, the duty on the financial planner was to ensure the proponent understood the importance of the questions and provided full and considered answers to the questions, not necessarily in the context and constraints of an on-line application process that provided little or no opportunity for an unsophisticated person such as Mr Stevens to reflect on the significance and accuracy of what was being put forward on his behalf to the insurer before he signed the document and submitted it for approval."

The judge stated that the financial planner:

- should have placed the best interests of Mr Stevens ahead of his employer's interests and his own interests;
- owed a fiduciary duty to his client, and particularly so as Stevens faced the risk of having no insurance at all if disclosure on the new insurance proposal proved insufficient;
- ought to have been particularly diligent and prudent as Stevens was an unsophisticated client and would not have been aware of the esoteric nature of replacing one insurance contract with another and the inherent risks in doing so.

The outcome

The judge ruled that CommInsure was justified in avoiding the policy under section 29 of the Insurance Contracts Act 1984. The Act states that an insurer can avoid (i.e. rescind) an insurance contract if the insured failed to comply with the duty of disclosure or made a misrepresentation to the insurer before the contract was entered into. This does not apply if the insurer would have entered into the contract, had it not been for the failure to comply with the duty of disclosure or the misrepresentation. This caveat is to ensure insurers do not avoid contracts for a failure to disclose innocuous information which would not have materially impacted the risk that the insurer was taking on.

If the insurer would not have been prepared to enter into a contract of life insurance with the insured on any terms if the duty of disclosure had been complied with or the misrepresentation not been made, the insurer may, within 3 years after the contract was entered into, avoid the contract.

The judge also found Commonwealth Financial Planning, as second defendant, negligent and guilty of misleading and deceptive conduct. They were ordered to compensate Stevens for the amount of $311,128. Three days after this finding was handed down, Noel Stevens died. Commonwealth Financial Planning subsequently appealed the decision and lost.

Here are some excerpts from the judge's considerations:

1. "In the circumstances, the duty on the financial planner was to ensure the proponent understood the importance of the questions and provided full and considered answers to the questions, not necessarily in the context and constraints of an on-line application process that provided little or no opportunity for an unsophisticated person such as Mr Stevens to reflect on the significance and accuracy of what was being put forward on his behalf to the insurer before he signed the document and submitted it for approval".

2. "In my view, given the risk to the proponent in the event of a material non-disclosure, a reasonable person in the position of [the financial planner] ought to have printed off the form or produced an equivalent hard copy for Mr Stevens to consider and complete carefully, including by taking it away if necessary in order to check medical matters, before it was submitted to the insurer."

3. "Furthermore, when the requirements of s 5D of the CL Act are considered from the perspective of causation of loss, in my view it is plain that were it not for the negligence, as I found to have been the case here, it would have been unlikely that Mr Stevens would have accepted the risk of the possibility of an avoided policy by surrendering one that was perfectly good and acceptable to him and where it was within the scope of the duties of a financial planner giving an unsophisticated person advice to ensure that the person in question was being given recommendations that were in his best interests, without conflict arising with the interests of the seller of the products being recommended".

4. "The conduct of the second defendant, by its representative [the financial planner], in providing an inadequate opportunity for Mr Stevens to read and understand the disclosure documents and the statement of advice created a circumstance where it was likely, as I find to be the case, Mr Stevens was misled and deceived into thinking that he was protected by his new policy arrangements when, by reason of the limited opportunity for disclosure, it is clear that he was not."

Key points for advisers

This case highlights the not insignificant risk of replacing a perfectly good existing insurance contract with another, particularly if the existing policy has been in force for some years. There are several key takeaways for advisers from this case.

1. Be careful about making statements to justify the product replacement, whether oral or written, such as "it would be better for you to have all your products with the one service provider". This is not likely to represent an advantage of any significance at all to the client and could be perceived as misleading.

2. Be careful about making statements to a client such as "I can do a better deal on your existing life insurance policy". Such statements can be considered misleading and deceptive. Premium comparisons and quotation estimates represent best case scenarios of insurance pricing for a client, particularly if they end up being assessed with premium loadings and exclusions, or even worse, they end up with a new policy that can be avoided due to innocent non-disclosure. Take a more cautious approach in terms of any statements you make.

3. Advisers ought to make it very clear to their clients at the outset that there is a risk if material non-disclosure can be retrospectively demonstrated at the underwriting stage, in that the insurance contract can be avoided and set aside by the insurer. At a time of claim your client may be left without any cover. What is the point of having insurance in the first place if this is the outcome? In this case, Stevens was unaware of the seriousness of non-disclosure, or in fact what it even was. Ensure the proponent understands the importance of the questions being asked, and that they provide full and considered answers to the questions.
4. Tailor your approach with clients that are elderly, less financially savvy or not as well-educated. Stevens was not a well-educated man and clearly would not have appreciated the finer points of insurance contract non-disclosure, misleading and deceptive conduct, or contract law. Take the time to state the obvious, in language they can understand.

5. Pre-warn your client about the likely questions they will face in the insurance application process; this way they are not stumbling to recall historical information and formulate on-the-spot answers during the insurance application process. Their health may be fine at the time they are applying for the new policy, but insurers need detailed information about past visits to GPs as well as past symptoms someone may have experienced but perhaps did not think it relevant at the time to consult a GP. Perhaps even get your client to ring their GP for a quick rundown on what consultations they have had over the last 5 or so years. I'm sure that in Stevens' own mind he knew his history of health was not unblemished, however he likely viewed most or all of his past health issues and symptoms as fairly innocuous in the overall scheme of things, and hardly life threatening.

6. Ensure your client reads both the Statement of Advice and the Product Disclosure Statement before proceeding with the recommendation. Bearing in mind it is highly unlikely that a client will read both documents in their entirety during the 'SOA presentation' meeting, perhaps it is best to leave the insurance application process for a follow up meeting. The judge in the above case was highly critical that the planner squeezed the entire advice and insurance application process into one meeting and put Stevens under a perceived time constraint when there was no legitimate reason to do so.

7. Ensure your client can review their answers to the questions in an online insurance proposal, preferably before submission, or within the cooling-off period and before they cancel their existing policy in the case of policy replacement advice.

Replacing an insurance policy can be a very risky business. Ask yourself "am I really recommending a like-for-like policy replacement?" Ask yourself "If I had to personally pay the client the sum insured in the event of a claim, what things would I want to know about the insurance applicant and their health history?"

If I was to enter a legally binding contract with someone to pay them thousands or millions of dollars in the event of a certain medical diagnosis, there is not much about their entire personal history I would not want to know, medical or otherwise. **FS**

Source: Rainmaker Technical Services Team

Stevens v Colonial Mutual Life Assurance Society Ltd (CommInsure) & Commonwealth Financial Planning Ltd [2012] District Court of NSW 94 (3 July 2012

The quote

The CBA financial planner failed to adequately inform Stevens of the consequences of potential material non-disclosure of health and related matters.