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Law and Practice – Australia

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AUSTRALIA

LAW AND PRACTICE: p.3

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The 'Law & Practice' sections provide easily accessible information on navigating the legal system when conducting business in the jurisdiction. Leading lawyers explain local law and practice at key transactional stages and for crucial aspects of doing business.

DOING BUSINESS IN AUSTRALIA: p.10

Chambers & Partners employ a large team of full-time researchers (over 140) in their London office who interview thousands of clients each year. This section is based on these interviews. The advice in this section is based on the views of clients with in-depth international experience.

Law and Practice

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Contributed by HFW ***Authors:*** Richard Jowett, Phil Kusiak

HFW is a sector-focused firm, recognised internationally as an industry leader, advising on all aspects of aviation, commodities, construction, energy and resources, insurance and reinsurance, and shipping. Through our integrated global network of offices, we offer a comprehensive range of dispute resolution, transactional and regulatory legal services to the insurance sector, including insurance and reinsurance companies; policyholders; captives and mutuals; brokers and other intermediaries; managing agencies and MGAs; TPAs and other service-providers. Our insurance and reinsurance work is high-value, likely to be complex and multi-party, and often international in nature. The specialist insurance and reinsurance team comprises 20 partners and more than 40 lawyers, of which four partners and ten insurance lawyers are based in Australia (Melbourne, Sydney and Perth). The firm has an extensive network of legal contacts, experts and correspondent firms whom we can mobilise, as required, worldwide. the firm's lawyers have in-depth industry knowledge and legal expertise. Several of our partners have worked directly in the insurance industry. Our work focuses on the most complex and high-value of insurance matters. Generally, we focus on matters that are multi-layered, cross-border, and involve multiple jurisdictions. We act for many of the most important insurance buyers and sellers in the Australian and international markets, as well as major insureds.

Authors

Richard Jowett is head of Asia Pacific Insurance and Reinsurance, and is deputy Industry Group Leader for Worldwide Insurance and Reinsurance. Richard covers insurance and reinsurance and, in particular, he handles high-value and/or complex claims. With a strong background in professional indemnity and liability work, Richard has branched into marine, construction, energy and ISR (including business interruption, delay in start-up, and ALOP). He is highly experienced in both direct insurance and reinsurance/retrocessions. Current high-profile matters in which he is instructed include the Tianjin explosion in August 2015 and various high-value Queensland flood claims. He also acted for one of the defendants in the Victorian bushfires class action litigation, having acted for the same client during the Royal Commission. He also advises on brokers' E&O, Directors & Officers' liability, insurance architecture (including captives) and contract certainty. A pragmatic, commercially minded and straight-talking lawyer, Richard aims first at understanding a client's objectives, and then developing and implementing a strategy to get the client to where they want to be. Richard is accessible, dedicated and a natural team leader with the organisational skills and capability of developing the right team for a client's purposes and then delivering the necessary results. These attributes have won him many awards judged by clients. He is a member of the Chartered Institute of Arbitrators (CIAB), a member of the Australian Insurance Law Association (AILA), an associate member of the Australia New Zealand Institute of Insurance and Finance (ANZIFF) and is dual-qualified in Australia and England.

Phil Kusiak is a senior associate and specialises in insurance-related litigation and dispute resolution. He has experience in high-value and complex insurance matters involving public and product liability, professional indemnity, directors' and officers' liability and contractual and statutory indemnity disputes. He also has experience in cross-border coverage analysis, defence litigation and subrogated recovery claims arising from catastrophic incidents in Australia and overseas. Phil has acted for multi-national private and publicly listed companies in the construction, mining, property, transport and logistics industries in a wide range of contentious matters. He has acted for insureds, leading insurers/reinsurers, captives and mutual insurers in claim presentations, coverage disputes, personal injury, property damage and professional negligence claims, civil procedure inquiries and statutory recovery actions.

1. Regulation

1.1 Regulation of Insurers and Reinsurers

The Australian Prudential Regulation Authority (APRA) is the Australian financial services industry regulator. The Australian Securities and Investment Commission (ASIC) is the consumer protection regulator. The Insurance Act 1973 (Cth) provides that APRA determines the prudential standards for general insurers and non-operating holding companies of general insurers in Australia. APRA also oversees regulation of banks, credit unions, building societies, general insurance and reinsurance companies, life insurance, private health insurance, friendly societies and most members of the superannuation industry.

A general insurer is a body corporate (or a Lloyd's underwriter) which has been authorised by APRA to carry on an insurance business in Australia. In order to obtain authorisation, the body corporate will need to meet certain minimum requirements. These include demonstrating that (i) the directors and senior management are fit and proper, (ii) minimum capital requirements have been met, (iii) risk management and control frameworks are adequate, and (iv) a certain value of assets is held in Australia by the applicant. Unauthorised foreign insurers may issue insurance in Australia only on certain grounds, including risks that cannot reasonably be placed in Australia.

The authorisation process also requires compliance with APRA's prudential standards and other regulatory and legal requirements. For example, insurers are required to submit a reinsurance management framework, which must include a reinsurance management strategy (REMS). The REMS is a high-level strategic document that sets out the key elements of the framework, along with supporting policies and procedures. These policies and procedures are then assessed by APRA to determine the adequacy and appropriateness of the measures.

A foreign-incorporated applicant which wishes to operate in the Australian market may seek to establish a locally incorporated subsidiary to carry on insurance business in Australia (known as a foreign-owned subsidiary). Alternatively, a foreign-incorporated insurer may seek authorisation to operate in Australia through a branch (known as a foreign insurer).

Foreign-owned subsidiaries and foreign insurers are subject to similar legislative and prudential requirements to locally incorporated general insurers. APRA does not, however, impose any restrictions on the number, size or mix of operations of foreign-owned subsidiaries or foreign insurers operating in the Australian market.

Insurers, brokers and other distributors must also hold an Australian Financial Services Licence (AFSL), issued by ASIC, or must themselves be authorised by a licencee. Reinsurers operating outside Australia are not required to register with APRA or hold an AFSL.

1.2 Domestic Developments and Impact of Standards

See above **1.1 Regulation of Insurers and Reinsurers**.

2. Distribution

2.1 Insurance and Reinsurance Products

Consumer Insurance

Consumer insurance is marketed to Australian consumers directly and generally without restrictions. In particular, home and contents, health, automotive and life insurance products are often advertised directly to consumers.

In addition to a government-funded healthcare system known as Medicare, consumers in Australia may supplement their healthcare with private health insurance, with high-income earners offered tax incentives to purchase private insurance. Health insurance is generally written by sector-specific insurers, with various comparison agencies connecting consumers and providers. Certain employers also offer their employees reduced premiums on private health insurance as part of their employment entitlements.

Like health insurance, automotive insurance is issued by automotive-specific insurers, although recent years have seen the emergence of automotive insurance issued through new entrants, including national retailers Coles and Woolworths. These policies, however, are often underwritten by national insurers and/or the Australian arms of international insurers. Other insurers are offering tailored, low-cost vehicle insurance with premiums based on the consumer's vehicle usage and/or parking conditions. Vehicle owners/drivers are required to have compulsory third party (CTP) insurance to cover their legal liability for personal injury to third parties. As the name suggests, CTP insurance is compulsory, however the purchasing of such insurance varies from state to state. Generally, the cost of this insurance is included in an annual vehicle registration fee paid to the relevant state or territory government.

Workers' compensation insurance schemes covering workers (and employers in respect of their legal liability to those workers) are also operated by federal and various state and territory governments, with points of difference between each scheme. In Western Australia, for example, the scheme is funded through premiums paid to private insurers, whereas in Victoria the scheme is centrally funded. The Commonwealth scheme, known as Comcare, covers employees of Commonwealth government agencies and statutory authorities, the Australian Capital Territory Government and corporations or authorities who have been granted a licence to self-insure.

Life insurance in Australia is structured around four main policy types:

- life cover (lump sum benefit upon death or diagnosis of a terminal illness);

- total and permanent disability cover (lump sum benefit upon total and permanent disability);
- trauma cover (lump sum benefit upon diagnosis of a critical illness); and
- income protection cover (replacement income if you are unable to work due to illness or injury).

These insurance products are often advertised directly to consumers and may be provided individually or in combination with one another. More recently, superannuation funds and retail banks have been offering life insurance products to their existing customers, often at discounted rates.

Home and contents insurance policies are often sold directly to consumers and can include added cover for specific high-value items and/or public liability risks. In some cases, these policies can be bundled with other insurance products, such as automotive insurance, with some of these bundles being sold through other financial institutions such as banks.

Corporate Insurance
A broad range of corporate insurance is both issued by Australian insurers and purchased by Australian-based corporate entities.

On the smaller end of the scale are insurance products for landlords, tradespeople and small businesses. As is commonplace in developed economies, medium and large businesses often purchase a number of insurance products, ranging from general liability insurance, to directors and officers liability insurance, to property damage/business interruption insurance. This insurance is often able to be placed in Australia, however the relatively small size of the Australian market means that larger policyholders often look to write a portion of the risk in foreign markets through non-Australian insurers and reinsurers.

Corporate insurance products are commonly sourced through brokers or sold directly by insurers. Certain markets, such as Lloyd's, permit licences to domestic coverholders and underwriting agencies which enable Australian organisations to place risk at Lloyd's with relative ease.

Market Players
As of 30 June 2016, there were 108 authorised Australian insurers, behind whom sit 191 individual reinsurance groups. Just over half of reinsurance recoverables in Australia are from intra-group reinsurers (being parent companies or related insurers), with the remainder being external reinsurance, comprising domestic, foreign and Lloyd's insurers.

A number of third party claims handling organisations also operate in Australia to provide foreign insurers with claims management services for domestic claims and insureds.

3. Overseas Firms Doing Business

3.1 Overseas-based Insurers and Reinsurers
In limited circumstances, it is possible for foreign insurers to operate an insurance business in Australia without authorisation from APRA. These insurers are known as unauthorised foreign insurers (UFIs), although they may only provide insurance contracts for atypical risks, high value insureds, and other risks that cannot reasonably be placed in Australia. All other insurance business will require APRA authorisation.

Reinsurers, foreign or otherwise, do not necessarily need APRA authorisation to provide reinsurance recoverable to insurers. However, the capital framework for general insurers imposes higher capital requirements for reinsurance recoverables from non-APRA authorised reinsurers relating to older events.

Although there are 191 reinsurance groups that provide reinsurance to the 108 authorised Australian insurers, the majority of reinsurance is placed with a select group of reinsurers, where three-quarters of Australian insurers' reinsurance recoverables are connected to one of ten reinsurer groups.

Reinsurance recoverables are also largely placed externally to Australia, with only 14% of Australian insurers' reinsurance recoverables connected to reinsurers based in Australia. Approximately half of these recoverables are related to reinsurers in Germany or Switzerland, with a further 20% placed with US reinsurers and 16% with reinsurers based in other jurisdictions. However, the proportion of reinsurance placed with European reinsurers is shrinking, in favour of reinsurers in the Americas and Australia.

4. Transaction Activity

4.1 Mergers and Acquisitions' Activities
In 2016, there was a global decline in the volume and total value of merger and acquisition (M&A) deals in the insurance sector compared to 2015. This was generally attributed to the strong political uncertainty resulting from the US election and the Brexit vote. In addition, the market was absorbing the massive deal between ACE Limited and Chubb Corporation, which was announced in 2015 and executed by early 2016. The deal involved a USD28.5 billion acquisition of Chubb Corporation by ACE Limited and was the largest international insurance M&A deal in recent years.

Despite the lack of growth in 2016, Australia has seen a variety of large deals in recent years, including Nippon Life Insurance Company's AUD2.4 billion acquisition of an 80% stake of MLC Limited in 2015. Other examples include the AUD1.84 billion acquisition of the Wesfarmers underwriting operations by IAG in 2013, and the AUD1.01 billion acquisition of Wesfarmers Insurance Brokerage operations by Arthur J. Gallagher in 2014.

Recent data suggests that, this year, Australia's general insurance sector is being pressured by significant claims cost increases to some business lines and tipping premium rate increases. Furthermore, organic growth has been difficult to generate and interest rates remain at historically low levels.

Accordingly, insurers may look to business acquisitions which will help them overcome the lack of growth. Insurers are likely to consider acquiring not necessarily other insurance operating entities, but other types of businesses which have accretive value and provide alternate avenues of distribution. It appears that many insurers are now investing in insurtech; however, as discussed below, this area has its own advantages and disadvantages.

5. Insurtech

5.1 Insurtech Development and Collaborations

In recent times, financial technology, or "fintech", has altered the landscape of the financial services industry by disrupting status quo business models and providing innovative new ways for customers to interact with service providers. Though the insurance industry has somewhat lagged behind other financial services in this area, it is no exception to the trend.

In the USA, innovators have already began to disrupt the insurance industry through "insurtech" developments. The application of insurtech in the insurance industry is quite broad and examples include companies providing peer-to-peer insurance and drone insurance policies.

However, the Australian market does not presently have the same access to investment capital as the USA and as such, the insurtech industry has not grown to the same extent. Nonetheless, the success of the first Australian Insurtech Conference, hosted by the Australian and New Zealand Institute of Insurance and Finance (ANZIIF), indicates that an influx of insurtech innovation is on the horizon.

Many of Australia's major insurers have indicated an intention to invest in and promote their own insurtech developments. For example, QBE Insurance Group has said that it would invest AUD50 million into partnerships with insurtech companies across four different countries. Meanwhile, Suncorp Group has bought a USD5 million equity stake in a US-based micro-insurance start-up and teamed up with Spanish start-up Traity, which uses Blockchain to protect consumers conducting peer-to-peer online exchange.

5.2 Regulator's Response to Insurtech Issues

The main obstacle hampering the expansion of insurtech in Australia is the lack of development in the regulation sector of the industry. The current regulations imposed by APRA make it difficult for domestic and overseas insurtech start-ups to flourish in the Australian market.

Last year, APRA announced that it would widen the types of fintechs that could operate within its regulatory space. However, progress has been slow and start-ups are, for the most part, still required to tag on the back of major insurers to get their products to the market. Although there are still limits on the growth of insurtech in Australia, APRA appears to be moving in a direction which is likely to benefit such companies and innovations in the future.

6. Emerging Risks and New Products

6.1 Risks and Regulator's Reponse to Risks

Cyber Attacks and Data Breaches

Both global and domestic cyber attacks continue to attract significant attention. The Petya and WannaCry ransomware attacks in mid-2017 affected the Australian branches of international companies, including those in the transport, communications and manufacturing sectors.

However, of equal significance for companies operating or looking to operate in Australia is the growth of cyber attacks targeted at domestic Australian organisations. Such incidents include attacks on the Australian Red Cross Blood Service, where personal records of approximately half a million donors were accessed by an unauthorised persons, and numerous phishing scams aimed at the national postage corporation Australia Post.

As data breaches continue to be an attractive target to perpetrators, the vulnerability of Australia's financial institutions, many of whom are engaging in strategies which will store and process data externally, is likely to increase the occurrence of attacks. This security surrounding external data holders is a cause for concern.

Australian CEOs now rate cyber threats as the equal greatest threat to the growth of their organisations, with the average cost of a data breach affecting Australian companies at approximately AUD2.8 million.

Although consumer appetite for cyber insurance has grown, its uptake is still relatively low. This is likely due (at least in part) to misunderstandings of the nature of the risk in certain industries and/or the difficulty brokers face in matching policies to those risk.

Catastrophes and Climate Change
Major catastrophes, often in the form of bushfires, floods and cyclones, are a relatively common occurrence in Australia.

Unique "new" catastrophe risks are not a particularly common risk written in the Australian market, although such insurance can be placed through foreign insurers not authorised by APRA where the insurance is to cover "atypical risks" (such as nuclear or biological hazards risks).

Climate change risks also present possible exposures for insureds and insurers, with speculation that the impact of climate change on business (such as the increased frequency of extreme weather events) may give rise to significant high-value litigation and/or class action proceedings.

6.2 Addressing the Emerging Risks
Arrangements are currently underway with various levels of Australian governments to trial automated vehicles on Australian roads. The implementation of autonomous vehicles for widespread public use will depend on whether, and if so, how agreements can be struck between state and federal governments with respect to the relevant vehicle licensing and safety authorities within each jurisdiction. This area of automation will undoubtedly see the development of new insurance products to meet the needs of consumers and organisations in the future.

A number of insurers have also expanded their offering to capture insurance for start-ups, including the CGU and Willis joint venture StartUpCover.

7. Recent and Forthcoming Legal Developments

7.1 Legal Developments and Impact
Reforms in the Life Insurance Industry
The life insurance industry is regulated by both APRA and ASIC. The general administration of the Insurance Contracts Act 1984 (Cth) (ICA) in the industry is within ASIC's purview. Under the ICA, insurers and policyholders must act towards each other with utmost good faith. The ICA also sets out a life insurance consumer's duty to disclose certain information when applying for a life insurance policy.

The Insurance Contracts Amendment Act 2013 (Cth) amended the remedies for the insurer in the case of non-fraudulent disclosure by the consumer. Consequently, rather than being able to avoid a policy within the first three years in the event of non-fraudulent disclosure, the insurer can alter the sum insured or vary the contract as if the non-disclosure or misrepresentation had not occurred. The reforms also further extended ASIC's capacity to take action where a life insurer fails to act in accordance with the duty of utmost good faith.

In addition, the Review of Retail Life Insurance Advice Final Report (known as the Trowbridge Report) of 2015, saw the development of a Life Insurance Code of Practice, modelled on the General Insurance Code of Practice. The Code sets out the minimum standards for compliance by life insurers. All life insurance companies which are members of the Financial Services Council were required to be fully compliant with the Code by 1 July 2017.

In recent years, the focus on regulatory reform has been on issues relating to remuneration of insurers and the quality of advice given to consumers. ASIC and the Joint Parliamentary Committee on Corporations and Financials Services carried out two separate inquiries in relation to (i) identifying the areas where further reform and improvement is required and (ii) an assessment of life insurance practices in Australia. The inquiries were intended to determine if there are any systemic concerns that apply either to particular insurers or to the industry as a whole.

The ASIC inquiry found that while life insurers were generally paying claims, there were significant issues regarding claims handling. It was suggested that public reporting on life insurance claim outcomes was necessary.

The Parliamentary inquiry is currently underway and a final report is due on 31 October 2017.

Life Insurance Remuneration Arrangements
The Federal Government has also made various attempts to improve trust and confidence in the financial services industry. In order to solve the problems associated with poor quality of advice and certain remuneration arrangements, the Future of Financial Advice reforms introduced a prohibition on conflicted remuneration, such as commissions or benefits paid to licensees that might be expected to influence their recommendation of a financial product or financial advice. However, conflicted remuneration in relation to life insurance was exempt from this prohibition.

The introduction of the Corporations Amendment (Life Insurance Remuneration Arrangements) Regulations 2017 aims to improve the quality of advice in the sale of life insurance by removing the exemption of the conflicted remuneration prohibition in relation to certain life risk insurance products. The Regulations allow only limited exemptions for benefits paid in relation to life risk insurance products (such as level commissions or capped upfront commissions) and give ASIC the power to make further instruments to specify the percentages of acceptable commissions. The majority of these reforms will commence on 1 January 2018.

Bigger Picture
It is understood that the life insurance remuneration reforms are part of a larger reform process. ASIC and APRA are in the process of formal consultations in relation to a number of areas in both general and life insurance sectors. These include the administration of design and distribution of products, handling of insurance claims and publication of claims data, additional surveillance and education of insurance professionals.

An example is the enactment of the Corporations Amendment (Professional Standards for Financial Advisers) Act 2017. This Act sets out mandatory education requirements for existing and new advisers, supervision requirements for new advisers, the implementation of an exam to ensure a common benchmark in the industry, and continuous professional development requirements. Most of these requirements will commence from 1 January 2019.

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8. Other Developments

8.1 Promoting Alternative Risk Transfer

The Federal Government has recently established a mandatory data breach notification scheme. Under the scheme, organisations covered by the Australian Privacy Act 1988 must notify individuals who are at risk of serious harm following a data breach.

Finally, the Federal Government has asked its Productivity Commission to undertake an inquiry into competition in Australia's financial systems, which will review and scrutinise policies that are sold in connection with a vertically or horizontally integrated business model (such as home loan insurance packaged with mortgages or automotive insurance offered through car dealers). The Productivity Commission's final report is due in mid-2018.

Doing Business in Australia

Country Profile
Australia is ranked as the fifth freest economy in the world according to the Heritage Foundation's 2017 Index for Economic Freedom. The country is included as one of the best places to live in terms of healthcare, income and civil rights.

There is a general perception that the Australian economy has *"done better than most"* in the years since the Global Financial Crisis. The country's continued growth has been supported by a decade-long mining boom, which is largely due to the high demand for minerals from Asia.

The country's economic policy is increasingly geared towards Asia and it is a key participant in the Asia Pacific Economic Co-operation forum.

Business Culture
Market experts advise that foreign parties will need to seek approval from FIRB (Foreign Investment Review Board) when obtaining a substantial interest in, or acquiring, an Australian corporation. Sources suggest that seeking approval from the FIRB has a political dimension, *"outsiders will often see FIRB as being a less transparent organisation. They are not apolitical; rather they are a conduit for the views and concerns of the Australian Government."*

It is generally accepted that Australians have an admirable work/life balance. Businesspeople note that *"you may find yourself working late but you won't be able to contact people past 6pm or 7pm."*

Locals take pride in their reputation for being frank and honest. Communication is often informal and "*unvarnished*" in both social and business interactions, with sources suggesting that a "*less nuanced, direct approach*" is advisable in negotiations.

Legal Market
The Australian legal system is well regarded; however, locals recognise that the multi-jurisdictional court structure can initially seem *"complicated"* to newcomers. Experts advise that early decisions often need to be made about where a case should be heard and whether litigants should use the Federal Courts or a state's Supreme Court.

Historically, the 'Big Six' Australian firms have undertaken the majority of high-value transactions; however, *"there are a tremendous amount of options outside of Big Six, such as the offices affiliated to the British firms and other strong independent domestic firms."*

Regulatory System
The Australian regulatory system is said to be transparent and efficient, although there is a general perception that it can be difficult to navigate. However, parties who are used to undertaking M&A transactions in America and Western Europe should be *"very comfortable"* with Australia's sophisticated regulatory framework.

The Australian Competition and Consumer Commission (ACCC) has established a voluntary merger-control filing regime, which means that only mergers that raise genuine competition concerns are required to be notified. Sources report that this *"official informal"* process is subject to clear and detailed guidelines.

Fees and Billing Methods
Law firms normally charge hourly rates. However, both practitioners and clients observe that firms are becoming more open to fixed or blended fee arrangements, especially in the wake of the global economic crisis. Experts explain: *"We are in a tough market and there are not as many mergers as there were three or four years ago, so we are more open to fixed-fee arrangements."* Despite this, businesspeople stress that *"in other parts of the world, the client has a reasonable amount of pricing power, but that is not the case in Australia as the firms stick to their guns."*

For corporate matters and litigation, the hourly rate for both international and domestic partners is said to be between AUD600 and AUD800, with AUD800 regarded as the *"top end of the market."* The associate rate for transactional and litigious matters is reported to be between AUD350 and AUD500. Fees for property work, however, differ slightly; the hourly rate for a real-estate partner at a domestic firm ranges from AUD500 to AUD700.