10 July, 2019

Senator Slade Brockman

Chair
Senate Standing Committee on Economics (Legislation)
Department of the Senate
PO Box 6100
Parliament House
CANBERRA ACT 2600
AUSTRALIA

Dear Senator Brockman

RE: Treasury Laws Amendment (Putting Members' Interests First) Bill 2019

ClearView appreciates the opportunity to provide its views to the Senate Standing Committee on Economics on the *Treasury Laws Amendment (Putting Members' Interests First) Bill 2019* (the Bill).

Our comments relate to proposed changes to group life insurance inside superannuation contained within the Bill, specifically the requirement on superannuation funds to only offer life insurance on an opt-in basis in relation to accounts of:

- members who have balances below $6,000; or
- new members who are under 25 years old.

However, on transition, we suggest all existing members under 25 should be required to opt-in.

We would like to take this opportunity to both congratulate the last Parliament on removing group life insurance on inactive accounts and reiterate our continuing support for the measure as a good first step in addressing "zombie" group life insurance.

Group life insurance inside superannuation

ClearView fully supports the Government's life insurance measures as provided in the Bill.

Requiring young Australians and those with low account balances to consciously opt-in for life insurance inside super is sensible public policy that will go some way to protecting members and ensuring savings are not eroded by premiums on life insurance they often do not need and commonly cannot even claim on.

T +61 2 8095 1300 F +61 2 9233 1960
Level 15, 20 Bond Street, Sydney NSW 2000
GPO Box 4232, Sydney NSW 2001
clearview.com.au

ClearView Wealth Limited
ACN 106 248 248
ASX Code CVW

That said, ClearView submits that the Government's measures should be considered a first and important step towards a scenario in which life insurance in super becomes optional on an opt-in basis for all workers. Many workers beyond age 25, e.g. casual workers, either don't require the cover provided, the standard cover absorbs an excessive amount of their meagre savings, and/or it provides cover they can't claim on. By opt-in we mean some clear separate application or consent to take cover. Once given, it would be reasonable for the opt-in to be presumed to remain in-force indefinitely.

We believe that once the proposed changes have been bedded down say, 12 months after the commencement of key provisions (i.e. 1 July 2021), their effectiveness should be formally reviewed to consider the merits of requiring superannuation funds to only offer life insurance on an opt-in basis for all members.

The purpose of this submission is to detail ClearView's views on group insurance through superannuation and why we believe an 'opt-in' approach, as set out in the Productivity Commission's package, is preferable to the current opt-out arrangements.

1. About ClearView

ClearView is an ASX-listed financial services company providing quality financial advice and life insurance, investment and superannuation products and services. It includes a registered life insurer, funds management business, superannuation trustee and two financial advice (AFS) licensees.

ClearView's aligned advisers oversee $8.9 billion in funds under advice and $265 million of life insurance premium under advice. As a product provider, ClearView has $2.62 billion of funds under management and $240.7 million of annual premium inforce.[1]

2. Introductory observations - History

It is relevant to observe that many of the key elements of Australia's current superannuation funds and their structures were established in the mid-1980's and arguably reflect the world as it was over the ten years prior to that. The funds largely started life as genuine "industry" based super funds, established under various industrial awards, and focused on members related to particular industries. It is also arguable that they were largely designed for a full-time work-force, with most members working in one industry throughout their careers, on a full career basis – i.e. people working 40 hours a week, over a 40 year career. The current group life arrangements were suitable for the labour market structure of 30 to 40 years ago.

The world in 2019 looks very different: substantially higher and increasing part-time work; a growing trend towards casualisation of the workforce; rising female participation with careers

[1] All values quoted are as at 31 December 2018, as defined and provided in the company's half-year results.

of both women and men frequently placed on temporary hold due to parenting; and increasing levels of switching between industries over workers' careers.

It would be remarkable if a system designed for a world 40 years ago still met the needs of workers today without change. From ClearView's perspective, it doesn't. The automatic, opt-out group life insurance arrangements are now characterised by the shortcomings discussed below.

Furthermore, in considering these issues, public policy ought to recognise not only the requirements of a system that will meet the needs of people today, but rather meet the needs of the evolving workforce over the next 10-20 years.

3. Problems with automatic, opt-out group life insurance

Many workers automatically get a low level of life, total and permanent disability (TPD) and/or income protection cover when they join a public offer superannuation fund. According to Canstar, 83 per cent of employees receive the default death benefit cover offered via their super fund.[2]

These public offer super funds arrange this cover via "Group Life" policies (essentially wholesale arrangements where the super fund is the policy owner and the policy covers the fund members on a blanket basis). These funds, especially the large funds, have used their size to negotiate particular policy terms and lower margin premium rates relative to typical retail, advised life insurance premiums (measured in terms of the ratio of aggregate claims incurred to premiums paid).

However, there are significant shortcomings and pitfalls with group life insurance. While group life cover often appears prima facie 'cheaper' overall than buying corresponding cover via standalone retail policies, this cover comes with a number of underlying costs and also often means that the group and standalone retail policies are not directly comparable:

- One-size-fits-all: The 'standard' amount of cover provided, and its terms and conditions, are usually very limited; group life insurance in super usually only provides for $100,000 to $200,000 in cover. This compares with research by the Financial Services Council (FSC) which estimates full time workers on average earnings with young children should typically have at least $500,000 to $650,000 in cover. The typical default super fund cover provides only 20% – 30% of the cover needed.[3]

- Lack of member education or advice: A corollary of the above point, as shown via responses to various consumer surveys over recent years, is that many members seem to think the cover they have been provided by their super fund is 'sufficient'.

[2] See - https://www.canstar.com.au/superannuation/insurance-through-super-yes-or-no/.
[3] See Submission 64 by Rice Walker to House of Representatives Economics Committee, page 15, referencing its report to IFSA/FSC.

As indicated above, this is not the case for many members who end up underinsured as a result.

In effect, the very provision of the default cover seems to give many members a false sense of security, and/or the fact they have cover dissuades them from properly and carefully considering what their cover needs might actually be. In this respect, the behavioural consequence of the default cover does as much harm as good for many members.

- Members paying for product they don't or can't use: At the other end of the spectrum, many other members often do not know or understand that they have insurance via their superannuation fund so they don't know they are paying for it. Others who do know often don't know how much cover they have. Either way, there is a tendency for these members to not claim benefits they may be entitled to.

  Worse still, is that members can be covered for benefits they cannot even claim. For example, income protection cover typically requires a minimum level of employment to be eligible to claim. Many part time and casual employees end up paying premiums for cover that provides no benefits at all. Members on career breaks are also affected where funds continue to deduct premiums for unavailable disability benefits.

  Other scenarios involve members with multiple accounts (e.g. part time workers in multiple schemes – including situations where this is required under enterprise agreements) – paying for multiple insurance benefits where even if they can claim, they can only claim under one set of cover and not all of them.

  These common scenarios result in some of the lowest paid members seeing their super balances eroded and effectively paying useless premiums that merely subsidise the premium rates that are charged to others.

- The healthy subsidise the unhealthy. The automatic-acceptance nature of group life insurance means there are generally no medical exams needed to access cover, and no pricing differential between healthy and unhealthy lives (or indeed often between members with higher risk and lower risk occupations or past-times). The cost of this risk pooling is simply spread over a large, disparate group of people. As a result, some members - such as healthy young women - are disadvantaged and may pay more for group cover than they would for individual retail cover because they are forced to subsidise other higher risk workers. This is not clearly disclosed to members.

- Inherent cross subsidies within the model. The above points raise a number of inherent cross subsidies in the current typical "averaged out" premium basis adopted; healthy subsidising the unhealthy, those with restricted claim ability (e.g. part-time and casual workers) subsidise those that can claim in full (e.g. those lucky enough to have permanent, full-time work with an unbroken career in an industry). However, there are other inherent cross subsidies in the many benefit scales offered. For instance, it is common for benefit scales to include a fixed level of cover by age up to a specific point and this then reduces linearly to age (say) 65. This pattern of cover usually does not reflect the actual underlying cost of claims. Such benefit scales inherently involve members in different age groups cross-subsidising others in other age groups.

Some may argue that such cross-subsidies average out over time (young casual working members today cross subsidising older full time working members eventually become the older members that are cross-subsidised themselves). However, for this averaging to be realised it assumes the current structure is sustainable over the next 20-30 years, and all or most of the current young workers will become full time workers when older. This is an optimistic assessment given the dramatic changes Australia's workforce will likely experience over the coming decades.

In the meantime, there is no transparency around these many cross-subsidies.

Some industry players have argued (to their own self-interest) that under 25 year olds represent a significant proportion of claims. This is obviously false as all group life insurers have said that premiums will need to rise for those members retaining their insurances in the fund as the cross subsidy from young members and those that legally cannot claim unwinds.

- Illusory cost advantage: One of the advantages claimed for group life cover is that it is often less expensive than retail, advised life insurance. In practice there are three key reasons for this apparent cost advantage:

    - To the extent that many are paying for cover they can't claim on (or have restricted ability to claim), this over-payment by this (significant) group simply reduces the apparent rate paid on average. This is not a genuine advantage (if, say, 20% of retail customers paid for cover they could not claim on then retail rates could be reduced 20% to appear 20% cheaper).

    - The various other cross-subsidies noted above also confuse and distort what are often suggested as "like-for-like" comparisons.

    - Perhaps most importantly, a significant component of retail premiums is the cost to fund the provision of personalised financial advice supported by the product. Super fund members "save" on the cost of that advice – but they don't get the education, insight and advice that is appropriate to their specific circumstances, resulting in the wrong cover, inadequate levels of cover, or insurance that is not needed.

- No trauma insurance. Trauma or critical illness cover is not available through superannuation. This type of insurance provides a lump sum of money to cover short-term medical and financial needs and is commonly provided as part of retail, advised life insurance. As noted above, group life cover encourages people to think they are reasonably covered, regardless of their individual circumstances. The lack of trauma cover represents a key gap in cover many are exposed to as a direct consequence of the current one-size-fits-all approach.

It is ClearView's belief that under the current system, many workers have cover they don't know about while others think they're adequately covered when they're not. Some members are actually paying premiums for cover they can't even use. They aren't paying for advice and so don't get any, and they or their families have to bear the consequences.

If the goal of group life insurance is to protect and maximise value for members, this is a highly inefficient system. It hinders optimal behaviour by discouraging members from properly assessing their insurance needs and regularly reviewing their arrangements. Instead it facilitates a "set-and-forget" approach to insurance, giving members a false sense of security.

We believe that some of the shortcomings associated with current group life arrangements can be seen in a recent Annual Report of the Superannuation Complaints Tribunal (SCT) that states that complaints related to insurance and these policies has increased steadily over the last five years. These complaints rose to 9% of the total received by the SCT in 2015/16 from 4% in 2011/12.

The current approach may have been valid 30-40 years ago with the overall social benefits of the approach outweighing the then lesser costs of the weakness and inefficiencies. That is no longer true and is likely to become increasingly less true in future.

4. An opt-in system

As acknowledged in the Productivity Commission's recent review of the superannuation system, group life can inappropriately dilute member interests and current opt-out arrangements are not working well.

ClearView believes that a system which requires members to consciously opt-in for group insurance in super will result in a substantial improvement in understanding what they are, and aren't, covered for and how much cover they have. This will significantly reduce the number of workers who think they, and their loved ones, are adequately protected when they're not. Importantly it will lead to more workers seeking advice, either via their super fund or a third party, about the type, and level, of cover they need.

In this regard, measures contained in the Productivity Commission's final report *Superannuation: Assessing Efficiency and Competitiveness* ought to be welcomed and supported as an important first step in the broader implementation of opt-in for group insurance in super.

The alternative of making opting out easier doesn't help those who don't understand that they are paying for useless cover and who don't even consider that they should opt-out of it. In addition, inertia and member disengagement will likely mean it would have limited success –

indeed the lack of success in getting members to save fees by aggregating duplicate accounts should be instructive in this respect.

An opt-in model will also force many of the current inherent cross-subsidies to be addressed and help make transparent what the real costs of the current system are.

ClearView believes that an opt-in arrangement will go some way towards addressing Australia's chronic underinsurance problem. In a similar study to the FSC study referred to above, Rice Warner Actuaries estimates that the typical default cover in super only covers 30 per cent of a young family's needs in the event of the death of a parent. Sadly, too many people discover this only when they are paid a claim.

Underinsurance also impacts on government and public finances. Rice Warner estimates the total cost of life and disability underinsurance to government is over $1.5 billion per year. [4]

This does not count the broader costs to the community and society from the reallocation of private sector resources (families, businesses and the not for profit sector) in dealing with this gap.

Please do not hesitate to contact me if further information is required.

Yours sincerely,

[redacted]

Simon Swanson
Managing Director

[4] See - http://ricewarner.com/australias-persistent-life-underinsurance-gap/.