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Committee Secretary
Parliamentary Joint Committee on Corporations and Financial Services
P O Box 6100
Canberra ACT 2600

By e-mail to: corporations.joint@aph.gov.au

Dear Sir

SUPERANNUATION LEGISLATION AMENDMENT (FURTHER MYSUPER AND TRANSPARENCY MEASURES) BILL 2012

We refer to your Committee's inquiry into the above Bill.

Terminology used in this submission

Tranche 3 Bill	Superannuation Legislation Amendment (Further MySuper and Transparency Measures) Bill 2012
EM	Explanatory Memorandum to the above Bill
The Association	Corporate Super Association
SIS Act	Superannuation Industry (Supervision) Act.

Background: the Corporate Super Association

Established in 1997, the Association is the representative body for large corporate not-for-profit superannuation funds and their employer-sponsors. We represent 35% of corporate fund assets and 30% of members of corporate superannuation funds. In general, these funds are sponsored by corporate employer sponsors with membership restricted to employees from the same holding company group, but we also include in our membership a few multi-employer funds with similar employer involvement and focus.

Many of the funds we represent include defined benefit divisions. Many of the defined benefit divisions are closed to new members, but there are also several that remain open. Many of the members are entitled to a combination of defined and accumulation benefits.

Tranche 3 Bill

Our comments relate to insurance matters and in particular to:

- the proposed denial of ability of funds to cover certain risks;
- the desirability of continued self-insurance in relation to certain accumulation members.

These matters have previously been raised with Treasury. For reasons set out below, we do not concur with the views of Treasury and APRA regarding the reduction of risk through external insurance and the increase in risk through self-insurance.

Likewise, we do not concur that certain risks should not be covered because the insured benefits cannot always be released concurrent with satisfaction of release conditions in the SIS Regulations.

Removal of ability for funds to cover certain risks

We note the decision reflected in proposed paragraphs 31(2)(ea) and (eb) of the SIS Act and forthcoming regulations (foreshadowed at EM paragraph 2.24 to 2.28) that funds should limit their coverage to death, terminal medical conditions, total and permanent disablement and temporary disablement.

In our view, the flexibility to cover more than just life risk and disability risk would be desirable. Some employers have contractual arrangements to cover specific trauma and other occupation specific risks, and if removed from the fund coverage (where economies of scale and administration exist) the result will be higher cost for the employer and a need to re-negotiate employment terms, and also to address the difficulty of reduction in benefits under deed.

A further consideration is potential innovation in fund products. Longevity products in particular have been coming under attention as of potential value for trustees and fund members. The opportunity to innovate will be in the interests of members and should not be inhibited by rigidity.

Self-insurance

We refer to proposed section 68AA of the SIS Act and the proposed operating standards (referred to in paragraph 2.28 of the EM) which would prevent trustees self-insuring benefits consistent with the conditions of release for death, terminal medical condition, permanent incapacity or temporary incapacity in the SIS Regulations,

except where the fund is a defined benefit fund or scheme that is already permitted to self-insure in respect of defined benefit members by a condition on their RSE license.

We note and respect the argument that prohibiting self-insurance for accumulation funds will reduce the risk for other members, should the fund not maintain adequate capital resources to release unforeseen member claims, as well as ensuring that the insurance provided complies with the prudential requirements relating to insurance. We would not advocate self-insurance in a fund other than where the risks are suitably managed under appropriate advice.

However, our membership and its actuarial advisers are of the view that where an appropriate process is in place, the risks associated with self-insurance can be managed with very satisfactory results and in the best interests of members. Appropriate process will involve taking account of the size of the fund and the scale of its arrangements, the availability of reserves, and the availability of re-insurance and of catastrophe cover and the financial capacity of the employer sponsor.

We have a substantial fund in our membership that self-insures death and disablement benefits for accumulation members. The withdrawal of the ability to self-insure in this way would give rise to significant problems and prejudice fund members because:

- The occupation of the members is sufficiently hazardous that evaluation of risk and provision of coverage is highly specialist and is difficult or prohibitively expensive to obtain elsewhere. The funds' experience in the provision of the insurance in these cases is such that the fund, subject of course to other prudential factors, better placed than an external insurer to assess and manage the 'insurance' the risk;

- Some funds have particular definitions of TPD in their trust deed for which external cover cannot currently be obtained. Whilst we understand the drive to harmonise trust deed TPD definition with the insurance policy requirements, we believe that this approach fails to take into account the interests of employees and members of specific funds who are employed in particular environments and occupations and whose conditions of employment require particular consideration.

As a further matter, there is no protection for a trustee who will be required to reduce the benefits currently offered to members to meet the new requirements.

Arguments in favour of self-insurance

These include the following.

- Funds have experienced considerable delays in determining and paying claims by external insurers, whereas in-house arrangements result in early settlement of claims.

- The cost savings resulting from not having to pay for the external insurers' profit margins are considerable.
- A self-insured fund can adopt a policy of universal acceptance of risk for all employees (subject to monitoring of adverse selection), whereas an external insurer may well require exclusions and specific underwriting.
- Where the fund self-insures, the employer and the trustee can tailor the cover to what is meaningful to their employees.
- The experience of providing cover, evaluating risks and reviewing experience promotes a safety culture in a business. Feedback as to specific risks encourages the employer to mitigate those risks in the workplace.
- Because of specialist knowledge of the employer, its industry and its risks, certain funds are better positioned than many insurers to evaluate the relevant risks.
- Certain funds and their sponsoring employers have credit ratings that are competitive with or superior to the insurers they would otherwise be using.
- Employers whose work force spends time in overseas locations can experience complexity in providing insurance cover for those employees. The risks, if insured externally, may result in arrangements with a multitude of external insurers, and potential gaps in coverage. If covered by the Australian fund under self-insurance, risks are mitigated.

Residual risk for trustee

External insurance arrangements cannot in fact remove all self-insurance or liability from the trustee.

For example, if the insurer fails to pay up on a claim for a liability to which the trustee is subjected, the trustee will have to find resources to pay the claim nonetheless. This can occur in situations where the insurer manages the claims process and arrives at a different conclusion from that of the trustee (or from that of a Court or Tribunal). We question how it is proposed to deal with these situations if all coverage of death and disability risks is to be externally insured and no self-insurance is permitted.

As indicated above, there may also be situations where the deed provides for benefits that the Draft Bill proposes should not be provided. During the period of transition these benefits will have to be insured, self-insured, managed out and otherwise provided for by the trustee.

Common pool for accumulation and defined benefits

Many of the funds that self-insure provide cover for defined benefit and accumulation members. Some of these members are entitled to both defined and accumulation

benefits, some have hybrid benefits (accumulation in certain circumstances, defined in others).

The underwriting reserves are pooled, there are economies of scale, and the occupational and industry risks are the same, and the pool is a specialist pool of value to the employer, group or industry. If the ability to insure for accumulation members is removed, it will change the dynamics of such a pool, altering economies of scale and risk, and potentially damaging a valuable resource.

Self insurance for defined benefit funds

As regards defined benefit funds, we are also concerned by the proposal that only defined benefit funds that currently have self-insurance arrangements in place should be allowed to continue. Our members have pointed out that this removes the flexibility to bring insurance arrangements in house again. There may be compelling market and practical reasons for so doing. These include situations where cover is not available elsewhere or is too expensive; and the situation where insurers make adverse decisions leaving the trustee with residual liability.

Yours faithfully

Mark N Cerché
Chairman
Corporate Superannuation Association