AUSTRALIAN INSTITUTE of SUPERANNUATION TRUSTEES

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Senate Economics Legislation Committee
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CANBERRA ACT 2600

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In brief:
AIST submits that in its current form the proposed Treasury Laws Amendment (Putting Members' Interests First) Bill 2019 would be significantly detrimental to members and would undermine trust in the superannuation system.

AIST has recommended that;

- Insurance should remain in place for low balance members when the account is receiving contributions (active accounts);
- Allow trustees to offer opt-out insurance where they can demonstrate that it is in the best interests of their members or cohorts of members;
- Allow members to opt-in and retain insurance via methods such as a meeting, a telephone conversation and a written election;
- The application of the $6,000 balance at an account level rather than a product level; and
- To expand the employer-sponsor contribution exception.

In addition, AIST has called for a delay in commencement to 1 July 2020 to enable funds to comply and communicate effectively with their members.

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

The Australian Institute of Superannuation Trustees (AIST) welcomes the opportunity to make a submission regarding the *Treasury Laws Amendment (Putting Members' Interests First) Bill 2019* (**'the Bill'**).

AIST supports the provision of opt-out insurance through superannuation as a cost effective way way of providing basic insurance cover to the millions of Australians who would not otherwise have life or disability insurance, or for whom insurance would be more expensive or inaccessible. Following a death or permanent disablement, an insurance benefit can make a significant difference to people's lives and, without such insurance cover, there would be a higher reliance on Government-funded benefits.

AIST agrees that having multiple insurance policies through multiple superannuation accounts is an undesirable outcome, as it leads to the erosion of retirement balances. Accordingly, we supported the inactive account consolidation measures in the Treasury Laws Amendment (Protecting Your Superannuation Package) Act 2019 (**'PYSP'**) which came into effect on 1 July 2019. Importantly, this consolidation of inactive accounts should be allowed to proceed before further changes are made.

AIST also agrees that members should not be paying for insurance that they don't need. However, we have significant concerns that the *Putting Members' Interests First Bill* will also remove insurance cover from many members who need it. These members include:

- Under 25 or low balance members working in hazardous industries or occupations;
- Under 25 or low balance members where there is a strong history of claims on insurance through super;
- Under 25 or low balance members from demographics who are more likely to have dependents;
- People, particularly women, entering the workforce after raising families, whose balances have not yet reached $6,000, but who have dependents; and
- People, particularly women, who have low wages and/or broken or part-time work patterns, whose balances are less than $6,000, but who have dependents.

In addition, because of an increase in the costs of their premiums from age of 25 onwards, the measures will not result in a lifetime cost saving on insurance premiums for members for whom are not receiving insurance until they are aged 25.

AIST also has significant concerns that the timeframes in the Bill are so tight they are impossible to comply with. Even if, funds and administrators were able to comply, rushing further changes to insurance cover through superannuation as proposed in the Bill risks real and significant consumer detriment and may result in a loss of confidence in the superannuation system.

For these reasons we do not support the proposed Bill in its current form and believe that it would be significantly detrimental to members. AIST's recommendation is that:

Recommendation 1	Insurance should remain in place for low balance members when the account is receiving contributions (active accounts).

Despite this in principle objection, we recommend the following amendments to the Bill:

Recommendation 2	Delay commencement to 1 July 2020 to enable funds to comply and communicate with their members, and for the first round of account consolidation to occur.
Recommendation 3	Amend the Bill so that the $6,000 balance applies at account level rather than product level.

Recommendation 4	Allow trustees to offer opt-out insurance where they can demonstrate that opt-out insurance is in the interests of their members or cohorts of members.
Recommendation 5	Update the Bill to reflect the Explanatory Memorandum of the Bill which allows members to opt to retain insurance via methods such as a meeting, a telephone conversation and a written election.
Recommendation 6	Expand the 68AAE employer-sponsor contribution exception to include when an amount of at least 50% of all premiums (both employer and member paid) are '*met*' by an employer-sponsor.

Existing protections

It is understood that the purported objective of the Bill is to remove the impact of insurance premiums on retirement savings for affected cohorts. The Government – through PYSP, has recently introduced auto-consolidation of inactive low balance superannuation accounts and removed default cover for all inactive accounts. These changes, which were supported by the industry, effectively address the impact of insurance premiums on the retirement savings of members with inactive and multiple superannuation accounts.

Timing is unworkable, will create member confusion and undermine trust in the system

The proposed Bill expects a commencement date of 1 October and for trustees to notify affected members on or before 1 August 2019. Because the Bill cannot be passed before late in July, this leaves funds with virtually no time to comply. Clearly, the proposed timeframe is unacceptable, it is unworkable for superannuation funds and will exacerbate member confusion arising from the PYSP changes. This confusion will ultimately result in a growing lack of trust in the superannuation system.

It was only recently that, in order to comply with PYSP, funds were required to notify members regarding the cancellation default insurance for superannuation accounts that were inactive. Similar to the proposed Bill, PYSP had a short implementation time, which ultimately led to significant member confusion summarised below:

- Funds did not have time to develop broad member information campaigns or phase direct communications to members about the changes, creating significant member uncertainty;
- Members were anxious and call centres were swamped with member queries and requests to opt in, with funds reporting up to a 300% increase in call volumes and record call drop-out rates;
- Funds have reported unexpectedly high numbers (10% - 35%) of impacted members opting to maintain their insurance;
- Increase in complaints to both funds and to Australian Financial Complaints Authority (AFCA) related to the changes;

- Funds have reported numbers of members who missed the opt-in date requesting to have their insurance reinstated, and have concerns about members who were overseas at the time of the change, and members who are disabled or have other barriers to opting in; and
- Fund administrators are still implementing systems to automate the PYSP changes.
  This unnecessary time pressure on funds comes at a financial cost, which ultimately has a negative impact on members.

It can also be reasonably expected that at this time a number of members under the age of 25 and with an active balance below $6,000 would have been correctly informed that they were not going to lose their insurance. Under the Bill, these members will now lose their insurance cover.

Example – Uninsured Colin

Example Colin is 25 years old with a new born son and has recently purchased a new house. Colin has one active MySuper account with a balance of $4,000 and two small lost/inactive accounts with combined balance of $2,500

June 2019 – Colin is concerned that he will lose his insurance as a result of PYSP. He is correctly advised by his fund that his account is active, so he will not lose his insurance held within that fund.
August 2019 – As Colin has a balance of less than $6,000, he is now sent a letter being advised that he will lose his superannuation insurance.
December 2019 – Colin's lost/inactive accounts are consolidated into his active MySuper account by the ATO.
December 2019– Colin is now advised by his active MySuper fund that his insurance has been switched back on because his balance has reached above $6,000*.

Unfortunately for Colin, he suffers an injury in November and was left uninsured at this time

**It remains unclear how this will work in practice and how re-activation of insurance will apply differently for MySuper and Choice products. More guidance is needed.*

Another round of cancellation of default insurance, so shortly after the PYSP changes is highly likely to confuse members and further undermine trust in the superannuation system.

The updates to processes and systems required to identify members, develop an opt-in mechanism, draft, tailor, test for effectiveness, review and send notifications to members takes considerable time. In addition, the implementation of the proposed measures will require changes to fund documentation, such as Product Disclosure Statements and the distribution of Significant Event Notices.

In addition to the timing issues identified above, as a result of PYSP, consolidation of inactive balances to the ATO is expected to roll around $6 billion into members' active account in the first year, increasing balances in the active accounts of millions of members. The first tranche of inactive low balance accounts must be transferred to the ATO by 31 October 2019, and the second in 30 April 2020. These important processes should be allowed to occur before the Government makes any further changes to insurance in superannuation.

If the Bill is passed in its current form, members with active accounts with balances of less than $6,000 will lose their insurance cover only to quite possibly have it reinstated a few months later once their inactive account/s are consolidated with their active account. This is highly confusing and adverse for members and could easily be avoided by extending the Bill's implementation date to after the first rounds of inactive account consolidation have occurred.

In light of this myriad of concerns, we propose that commencement is delayed to 1 July 2020.

Example – Sophie reaching $6,000

Example Sophie is 32 years old with two pre-school children, and has re-entered employment after a lengthy break. She works part-time (25 hours per week) waiting on tables at a lunch time café, and is paid award wages and SG contributions by her employer. Sophie has no life insurance.

Based on her annual wage of $24,547, her employer contributes $2,332 to her default super fund each year. It is estimated that at the age of 34 that here estimated super balance reaches a balance of $6,594*, until this time she will have no death or TPD insurance.

**Using ASIC MoneySmart superannuation calculator. Based on investing in a Balanced investment option and a medium fee level.*

Low balance active accounts should retain insurance or changes will disproportionately affect women

As highlighted in our response[1], and a significant number of other responses to PYSP, there is no policy rationale for not providing insurance to members with a balance of less than $6,000, if they are actively contributing to their account.

If insurance cover only commences when a new employee builds an account balance of $6,000, this could take a new full-time member on an annual income of $50,000, approximately 18 months to build that balance unless they get a transfer in, and longer for casual and part-time workers who represent an increasing proportion of the workforce. Part-time employment now accounts for nearly one-third of total employment[2].

AIST submits that this arrangement will be detrimental to new employees, people who are entering the workforce after raising families, and is likely to disproportionately affect women who are more likely to have broken work patterns and to be employed on a casual or part-time basis.

[1] AIST (2019), AIST Submission to Treasury: Protecting Your Super Package. Available from: http://www.aist.asn.au/media/1173207/20180525_submission_treasury_protectingsuper_v1.5_final.pdf

[2] Reserve Bank of Australia (2017), The Rising Share of Part-time Employment. Available from: https://www.rba.gov.au/publications/bulletin/2017/sep/pdf/bu-0917-3-the-rising-share-of-part-time-employment.pdf

We also submit that providing active members with insurance from the time they join (as opposed to reaching a certain balance) will make it easier for individuals to understand when their cover will commence while also avoiding potential future underwriting issues.

Example – Confused and frustrated Emily
Example Emily is 22 years of age and currently on maternity leave. **May 2019** – Emily is notified that because her account is inactive her insurance cover will be automatically cancelled. **June 2019** – Emily reads that you can either make an election or make a contribution to your account it will be deemed active. Emily decides to make a contribution in order to keep her insurance cover and she wants to increase her balance as she is not being paid super whilst on maternity leave. **August 2019** – Emily is now advised that because her balance is below $6,000 her insurance cover will be terminated in October. **September 2019** – Emily is concerned about losing her insurance and decides to try and call her fund. However due to longer than usual wait times, decides to give up. **October 2019 –** Emily's insurance cover is cancelled. **November 2019** – Emily would like to reinstate her insurance cover but is required to apply individually. Emily is advised that she will have to pay higher premiums than previously available.

Case study – Fund A, an industry super fund
Fund A is a large industry super fund. Members aged under 25 pay 65c per week or $34 per year for death and long-term disability income protection insurance cover. Over the last decade, Fund A's insurance partners have paid a death or disability income benefit to a member aged under 25 every 12 days, on average. Fund A has 177,742 active members with a balance under $6,000. Approximately 75% of these members are women. Their average age is 36 years old. A majority of these members have dependents. Under the proposed changes, these members will potentially lose over $500,000 in combined default death and long-term income protection. It takes members of Fund A approximately 2 years to reach a superannuation balance of $6,000 - this reflects the industry sector Fund A services, and the low wages in the sector. Like most people, a majority of these members do not have personal insurance cover outside superannuation. Due to demographic factors, 6% of members of Fund A never reach a superannuation balance of $6,000. For these members, the insurance component of their super is far more valuable than the additional retirement benefit that would have accrued if they didn't pay the insurance premiums.

Drafting Problems with PYSP should be resolved in this BIll

Finally, drafting problems with the PYSP - which make it unclear whether the changes apply to individual super products or the members' total account balance - have been replicated in this Bill. In a note to the industry APRA have stated[3];

[3] APRA (2019), Initial compliance with the Protecting Your Superannuation Package requirements. Available from: https://www.apra.gov.au/protecting-your-super-package-frequently-asked-questions

The Government has indicated to APRA that it will pursue amendments to the Superannuation Industry (Supervision) Act 1993 (SIS Act) to ensure the Government's policy intent, which underpinned the PYSP legislative reforms, is achieved in two areas that have been raised by industry (see below).

APRA understands the Government will seek to amend the SIS Act to provide that:

1. *the legislative requirements allow for the aggregation of a members' interests in one or more products held within a superannuation account;*

The proposed Bill must be updated to address this problem or members who have multiple products with a total balance of more than $6,000 but product balances of less than $6,000 will be adversely impacted by the changes. For example, a member with two products valued at $5,000 each (total of $10,000) will lose their default insurance as the Bill is currently proposed.

We recommend that the Bill is amended so that the $6,000 balance applies at an account level rather than the product level.

Younger members already protected through the Insurance in Superannuation Voluntary Code of Practice

AIST supports special default insurance arrangements for younger members, including the provision of insurance on an opt-in basis for members below a specified age. We wish to highlight that this is the subject of detailed consideration in the Insurance in Superannuation Voluntary Code of Practice. The Code provides that:

4.10 For younger members, when designing benefits we will consider:

> *a) appropriate types and levels of cover, given that younger people are less likely to have children and other dependants or significant debt, and are more likely to require total and permanent disability or income protection, rather than death cover;*
> *b) the impact of premiums on members who typically have low account balances;*
> *c) the likelihood that younger members will be earning significantly lower salaries than older members;*
> *d) working patterns, which may be casual or part-time; and*
> *e) fair treatment of younger members, taking into account whether there is any cross-subsidisation by premium with older members of the fund.*
>
> *and as a consequence of the above considerations, it is expected that levels of cover or premiums will be lower for younger members than for the membership generally.*

Unlike the Code, the proposed legislation does not give trustees the capacity to consider the particular needs of their younger members and allow them to tailor their insurance offerings accordingly.

Many young members still have a need for life and disability insurance

The premise that cohorts of members under the age of 25 are unlikely to have financial responsibilities and therefore wouldn't benefit from life or disability insurance is unfounded.

A significant number of members aged under 25, particularly those living in regional and remote areas do have dependents. By not providing default life insurance cover to these members, loved ones may not be supported in the event of death or permanent disability of a member.

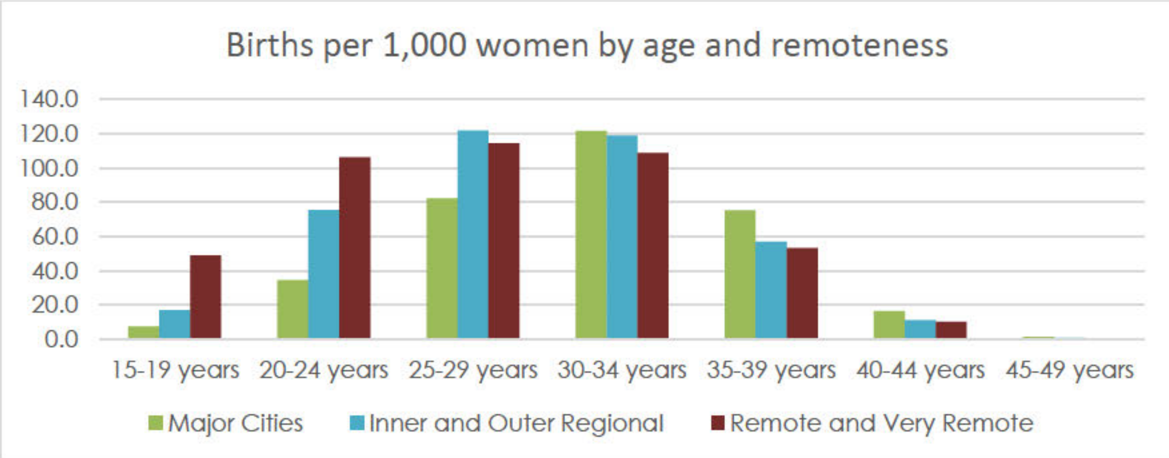

Figure 1: Australian Bureau of Statistics - Births, Summary, Remoteness Areas (2017)

Also, a significant number of members aged under 25 hold debt and would benefit from life insurance, protecting them so that the debt could be repaid in the unfortunate event of death or serious injury. In particular TPD and income protection insurance is vital to financially support young people who can no longer work due to illness or injury and would otherwise be dependent on public benefits.

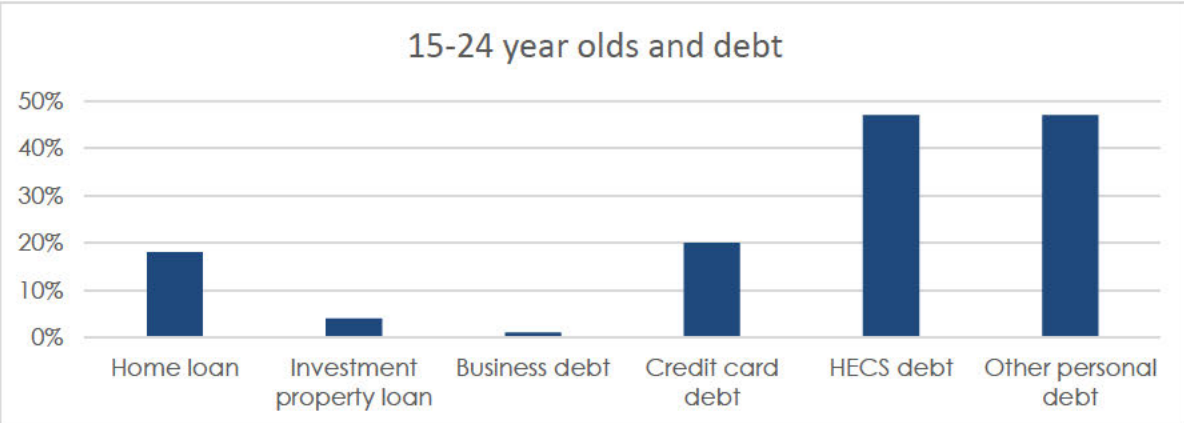

Figure 2: Reserve Bank of Australia (RBA) - E7 Household Debt Distribution (2014)

The same arguments hold true for members working in manual occupations, who tend to start working life and have family responsibilities at a much earlier age.

The Bill assumes that young Australians do not have financial responsibilities and rely on parents for financial support. This is despite considerable evidence that many young Australians also help their parents financially, particularly Australians born overseas. Surveys indicate that 64% of people agree that adult children should provide financial support to their parents if they need it (rising to 77% for those born in non-English speaking countries)[4].

Members working in hazardous industries need to be protected

In addition to those with dependents and debt, default insurance cover is also vital for members working in hazardous industries. If a member decides to opt-in then this will require individual underwriting. Due to underwriting, these members who need insurance are unlikely to be able to take out cover individually at an affordable price and may face detrimental exclusions or be denied coverage.

Sadly, members working in these high-risk industries are more likely to be involved in an accident and therefore have a higher need for insurance. According to Safe Work Australia, the industries with the highest number of serious injury claims in 2014-2015 were health care and social assistance, manufacturing and construction[5].

Although some have argued that members would be covered by WorkCover scheme's we note that there are significant differences between WorkCover and appropriate life, TPD and income protection insurance. WorkCover does not protect against injuries sustained outside of work, benefits are ambiguous and differ state to state. Further, it does not cover expenses unrelated to the injury (e.g. debt repayments or education bills) and tends to take longer and be more difficult for workers to make a successful claim.

Member Outcomes Assessment

The Government and the Australian Prudential Regulation Authority have recently introduced new requirements under which superannuation funds are required to annually assess member outcomes, including how each product continues to promote the financial interests of members. Obligations will also require a trustee to assess insurance and retirement savings outcomes achieved for members aged under 25 and for active members with balances of under $6,000.

APRA is responsible for administering these laws and can take regulatory action where a fund does not deliver valuable death and disability insurance cover to younger members and active members

[4] Australian Institute of Family Studies (2016), Attitudes towards intergenerational support. Available from: https://aifs.gov.au/publications/attitudes-towards-intergenerational-support
[5] Safe Work Australia (2015), Serious claims by disease and injury: Industry. Available from: https://www.safeworkaustralia.gov.au/statistics-and-research/statistics/disease-and-injuries/disease-and-injury-statistics-industry

with low balances, This is an important existing measure that ensures that trustees are striking an appropriate balance between the cost of insurance and members' retirement savings.

Opt-out group insurance for members or cohorts of members

We advocate that trustees should be able to provide opt-out group insurance to their members or cohorts of members when it is clearly in their best interest. Trustees would have an obligation to provide evidence that this cohort is at risk and that the default insurance is in their best interest. Evidence - such as an actuarial certificate - could be required to ensure that providing opt-out insurance is in the best interests of members.

This proposal would be in line with the Productivity Commission Inquiry Report which recommended[6]:

> *'exemptions to the under-25 opt-in restriction should only be granted if the trustee can demonstrate to APRA that opt-out disability or income protection insurance would be in the best interests of a specific cohort of younger members.'*

Method of electing to retain insurance must be broadened

Section 1.38 of the Explanatory Memorandum of the Bill states that 'A trustee will need to be able to demonstrate that a member has elected to maintain cover, for example, through a record of a meeting, a note following a telephone conversation, or holding a record of a written election'. In contradiction to this statement the Bill states that a member must make an election in writing. This contradiction provides unnecessary confusion and advocate that the Bill is updated to reflect the Explanatory Memorandum, allowing members to opt-in to retain insurance via other methods such as a meeting and a telephone conversation.

As highlighted earlier in our submission, during the implementation of PYSP members were anxious and call centres were swamped with member queries and requests to opt in, with funds reporting 50%-100% increases in call volumes and record call drop-out rates. This highlights that members value speaking to their funds for information and suggests that removing the ability for members to retain their insurance via a telephone conversation will result in a poor member experience and undermine confidence in the superannuation system. It may also result in members giving up and deciding that it is too difficult to retain much needed insurance.

Employer-sponsor contribution exception

The Bill should be amended to include a >50% threshold in relation to the amount of total premiums that are paid for by the employer. This would ensure that members continue to benefit

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[6] Productivity Commission Inquiry Report, Superannuation: Assessing Efficiency and Competitiveness (2018), 603. Available from: https://www.pc.gov.au/inquiries/completed/superannuation/assessment/report/superannuation-assessment.pdf

from comprehensive insurance cover, including where premiums are only part member paid, whilst still having their account balance protected from erosion through the deduction of insurance premiums. The only consequence of not providing a carve-out of this nature, would be to remove an employee benefit.

Limited increase in retirement balances and increased premium costs

Finally, we suggest that the presumption that removing default insurance cover for members under 25 and with a balance of less than $6,000 will make a significant difference to their retirement balance is flawed. In research on the economic impact of the PYSP and the impact of removing of default life insurance, actuarial firm, Rice Warner found that an individual's retirement balance is likely to increase by just $1,400 or 0.27 per cent over the course of their working life[7].

This is largely because the premium rates will increase as a result of these changes. Existing group life policies will need to be reviewed and repriced in light of the proposed changes. It is highly likely that these changes will force a significant increase in premium costs for a number of funds and consequently members. The short-time frame will also limit a trustees' ability to go to the market to negotiate the best deal for members with regards to their insurance benefits.

For further information regarding our submission, please contact [redacted]

Yours sincerely,

[redacted]

Eva Scheerlinck
Chief Executive Officer

The Australian Institute of Superannuation Trustees is a national not-for-profit organisation whose membership consists of the trustee directors and staff of industry, corporate and public-sector funds.

As the principal advocate and peak representative body for the $1.4 trillion profit-to-members superannuation sector, AIST plays a key role in policy development and is a leading provider of research.

AIST provides professional training and support for trustees and fund staff to help them meet the challenges of managing superannuation funds and advancing the interests of their fund members. Each year, AIST hosts the Conference of Major Superannuation Funds (CMSF), in addition to numerous other industry conferences and events.

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[7] Rice Warner, Economic Impact of 2018 Federal Budget Proposed Insurance Changes (2018). Available from: https://resources.aia.com.au/rs/482-ROS-457/images/Federal_Budget_Proposed_Insurance_Changes_%28AIA%29.pdf