22 May 2017

Insurance in Superannuation Working Group
Project Management Office
Via Email – ISWG-PMO@kpmg.com.au

Dear Sir/Madam

Discussion Paper: Account balance erosion due to insurance premiums

We wish to provide you the following submission in respect of the key questions raised in the above discussion paper.

At a high level:

- It is imperative that the final solution to address this challenge is all encompassing and covers the myriad of insurance arrangements (both current and future developed arrangements) an not be isolated to Income Protection arrangements
- Adoption of insurance cover levels or insurance fees (including insurance premiums) would not be in the best interests of members. It does not allow funds to provide insurance arrangements that are aligned to the type of membership base (nature of work, demographics etc.) they service, potentially resulting in members unable to access or lose cover, particularly female members who have broken work patterns, as well as casuals and part-time employees. In turn, increasing the burden on broader society, from drawing of government funds to increased medical and rehabilitation support from public funding as well as reduced available resources due to slower recovering to return to work that can be provided as support through the claims process.

Please find enclosed our detailed responses to feedback questions in the order posed within the discussion above paper:

B.1

1. Guidance on the determination of cover would be appropriate. This should be of a general nature only as to specifically tailor it to individual member cohorts would add unnecessary administrative burden and complexity.

2. Given the high prevalence and impact on female members who have broken work patterns, as well as casuals and part-time employees it would be difficult to tailor automatic cover at an individual level therefore a greater level of prescription would not be in the interests of individual members. Decisions need to be made taking in the considerations the membership as a whole.

3. Applying this approach to new members only would add significant complexity and confusion to existing members, not educe equity across membership base and unnecessarily lift the administrative burden.

4. The consequences to funds would depend on the level of prescription sought by principle – based guidance. Impacts on the distribution of cover and premiums would potentially have flow on impacts to loss ratios and the broader membership so care should be taken not to make this process overly complexed and also educe equity.

5. In reality, young and middle aged (45) members are a more appropriate segments of focus as the longer term cumulative impact on account balances would be greatest at these points. Older Australians are more likely to be more active in their superannuation decisions (including seeking to maintain existing arrangements) as they are more likely to

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recognise the importance of benefit entitlements. However in light of low engagement generally, care needs to be taken to making such assumptions of cohorts.

6. As per 5 “above”

7. Members particularly women with broken work patterns are likely to have suffered reduced account balances due to extended periods out of the workforce. It should be noted however the importance of insurance is not diminished in this group and to base or cap insurance arrangements in this way could unduly impact on this segment who recognise the importance of cover that protects the “unpaid but extremely valuable contribution” of this segment of Australians.

B.2

8. The definition should be general and should take into considerations the base circumstances of the average member. It would be incorrect to be too prescriptive particularly for the reasons outlined in 7 “above”

9. Consideration would be given to the impact of insurance premiums on the average account balance of a member given the part-time/’casualised’ and gender specific nature of our industry.

10. Yes, the female demographic has to be carefully considered. Unpaid household labour is extremely valuable and the necessity to provide insurance for employment of this nature cannot be understated. Prescriptive rules that apply based on cohorts rather than the “average” member could unduly impact on the identified needs of individuals of this nature where causal employment and broken work patterns are commonplace.

11. No. They should not be prescriptive or force cover to cease unnecessarily for the above reasons. Also, one must acknowledge that “ill” or “terminally ill” members may seek to maintain an account without receiving contributions as they are wanting to ensure they and their families have access to an entitlement as soon as they become eligible. Again prescriptive rules around ceasing cover can have unintended consequences as a result.

12. Assessment of thresholds should occur at the expiration of a rate guarantee. To do otherwise may have pricing implications for the broader membership if this were to result in changes to the underlying product offering and reduce confidence in the industry as a result of regular change that may occur from the review.

13. Whilst not supportive of maximus, the simplest approach is best. One maximum threshold limit would be preferable rather than causing the process to be unnecessarily complicated where the public already feel superannuation is confusing.

B.3

14. No, for the reasons set out in 7 and 11 above.

15. Whilst not supportive of thresholds, if the code were to prescribe a threshold the timeframe without contributions should be at least 24 months. This covers individuals who work casually with multiple employers and who choose to take a break for parental leave which has now been extended to 24 months under industrial law.

16. If a threshold is introduced it would be one threshold rather than multiple as this would increase administrative burden, complexity and confuse members.

17. 21 months would seem and appropriate time if a 24 month timeframe was prescribed by legislation.

18. No, cessation clauses introduce unnecessary risk for members. Given the heightened education around superannuation consolidation in recent years members may well be making an active decision to have multiple providers and insurance arrangements. For the reasons set out in 7 and 11 above, this introduces unnecessary risk that members who

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want and need cover may not respond to a communication from the Trustee within the required timeframe to continue cover.

19. While not supportive of mandatory cessation, at least 3 months after a 21 month notification period to align with the period individuals may take parental leave (i.e. up to 24 months)

20. Income protection is just one cover a member can have. Income protection can be offset for other income reasons such as transport accident and workers compensation. These features are priced in the cost of the cover for all members. Furthermore while TPD cover is not typically offset against other TPD policies this would lead to significant over insurance in some cases. It would be inappropriate to consider IP cover as an isolated insurance issue that needs to addressed. The issue of multiple insurance covers needs to be addressed holistically. Furthermore a number of funds are seeking to implement hybrid designs which are in the interests of their membership, so to consider IP in isolation would be inappropriate. Other socio economic factors also need to be taken into account including members' ability to manage lump sum benefits as there is some research undertaken by funds that the proceeds are spent quickly and not used for the period of time or purpose they are intended for.

21. Any consideration around cover automatically ceasing should address the concerns expressed in 7 and 11 above, this would have significant implications for members who have actively sought to maintain cover. It should also be noted that members may actually seek to maintain cover with one provider as they may not be able to transfer cover (due to health considerations) to an alternative provider. Careful consideration of the female demographic is paramount given broken work patterns and broader membership considerations where cover is ceased arbitrarily. This can introduce either anti- selection risks if cover is later reinstated, as well as having wider loss ratio implications based on a segment of the membership not having cover or paying premiums.

22. The MyGov site being used to advise members and facilitate the consolidated of cover across providers and the typical cost to their retirement savings to maintain this cover so members can make an informed decision when completing their tax return.

23. Administering cessation of cover provisions would be difficult and a number of members would ultimately be uninsured (particularly females with broken work patterns) or anti-selection risk would be introduced by introducing recommencement provisions which would not be in the interests of all members.

24. The insurance risks implications of ceasing and recommencing cover would be uncertain. Recommencement rules in isolation would work to introduce anti-selection risk so that members will be able to reactivate cover when they feel they need it most or they may be provided with cover that will not permit claims for pre-existing ailments as an anti-selection measure.

25. Ceasing cover would potentially mean that members with an identified need to claim will be active to maintain cover while others (for example members who do not pay adequate attention) would lose cover and any re-commencement rules may not reflect the cover removed so a member could be significantly impacted and lose important insurance benefits.

B.4

26. Careful consideration needs to be given to the fact members may actively maintain multiple covers to ensure the aggregate of cover from all sources adequately provides benefits for their needs. For example, a member may have IP cover with Fund A for $1,000 and Fund B for $1,000 and may have a pre-disability income greater than $2,000 so should obtain benefits from both providers.

27. The protocols should consider the sharing and co-ordination of assessment to avoid the need for multiple ongoing claim forms where the member seeks to and is eligible to claim from two providers based on their pre-disability income. It should also be considered that the terms and conditions in policies can be very different and this may impact on the best

interests of members where protocols are adopted. It should further be considered that the advent of hybrid policies (e.g. IP and TPD in one policy / benefit) may need to be taken into consideration in the adoption of any protocol.

B.5

28. Refunds would be too difficult to administer. There may be times where a member's pre-disability income is supportive of benefits from more than one provider in some circumstances. Income Protection can also be offset by Transport Accident Insurance and Workers Compensation insurance. It would be too simplistic to single out IP cover in these circumstances. A holistic approach to members having unnecessary cover through multiple providers should be considered rather than an isolated approach that seeks to address anomalies in IP cover in isolation. One must remember that IP cover is very supportive of a return to work strategy and is therefore a form of insurance that seeks to address the social good of continued employment. It also supports the growth in a superannuation account by addressing the long-term disability which is a product of Lump Sum TPD coverage. To single out IP cover as resulting in anomalies that need addressing in isolation would not acknowledge the social good that it seeks to address.

29. For the reasons expressed in 26-28 refund provisions for IP policies would add unnecessary complexity and would not be in the interests of members as a whole. Furthermore it would be inequitable to refund premiums only at claim time and it would be difficult to ascertain if a member's historical income could have justified a claim from more than one provider during a period of coverage as illustrated in 26 above.

30. If an industry standard on refunds is introduced this should be limited to no more than 24 months.

31. Significant administrative issues would be introduced for superannuation funds and insurers as there may have been historical instances where a member who is underinsured at more than 1 provider could have had an entitlement to at least partial benefited had they claimed from both providers.

32. This should not apply for the reasons expressed above (in 31) as significant complexity and inequity would be introduced by such an approach particularly if refunds were only instituted at the point of claim.

33. Yes, any approach that seeks to introduce refund protocols should have a considerable lead time (post current rate guarantee) as the administrative issues could be considerable. Further consideration would need to be given to the cost of administering insurance by the fund and what the potential extra administration insurance fee would do to premiums for all members that hold insurance cover.

C.1

34. Better education with relaxed advice provisions around the use of standardised calculators would assist members in making a better judgement about the adequacy of cover and could be used as a method to flag and encourage consolidation. More prominent messaging around consolidating insurance through providers should be standard within providers.

35. Disclosure of cover with each provider as well as their superannuation account balance with each on ATO published/accessible personal communications would drive awareness. Further, an insurance consolidation protocol across providers would aid in this regard.

36. Insurance, as well as superannuation balances should be reported to the ATO so as to facilitate consolidation through standardised protocols that address areas of policy concern. This would reduce the risk members may consolidate their super without fully comprehending the insurance implications.

37. Communication to members using their preferred contact method would facilitate messaging around the importance of consolidation of insurance arrangements.

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C.2

38. It would seem reasonable that a small timeframe (30 days) applies to prevent members establishing accounts unnecessarily. A period greater than this would still have the desired effect however members would conceivably be establishing new and overlapping arrangements for a short period of time before action can be taken by the member. It should be noted however that many members would work broken work patterns particularly in the female demographic. In many instances it may be part of their normal work patterns to have multiple concurrent employment arrangements or periods out of the workforce which would mean they may not be commencing a new employment arrangement in many circumstances. It should also be noted that the quarterly SG contributions cycle would tend to be problematic particularly in circumstances where members may have established and ceased multiple short term arrangements in this time period. In order to facilitate such a process it may be worthwhile if the Government were to reconsider the regularity with which contributions are required to be paid to minimise the existence of data timing gaps. Consideration should also be given to softening the rules in respect of Choice of Fund which currently only mandate that an employer need act on one request to redirect employer contributions to an alternative arrangement within a 12 month period.

39. The special needs for employees with broken work patterns would be particularly evident in the industry HESTA services as a number of members work casually or through multiple employers and the Fund's membership predominantly services the female demographic. There would need to be significant flexibility to cater for these members to avoid regular and unnecessary communications particularly where the member remains within the same industry sector. In these circumstances a longer notification cycle time could be warranted. It should also be noted that there would be a number of circumstances where members work casually and effectively remain on the books of an employer with the prospect of new assignments when they present themselves. In these circumstances employment termination for the purposes of reporting would need to be clearly defined and may in reality be an extended period (i.e. 3-6 months) of employment inactivity for practical reasons. Further, employees may not meet the minimum threshold if they work minimal shifts within the month and thus, whilst still employed, the employer is not required to make superannuation contributions.

40. Ideally communications to members based on defined known triggers such as the termination of employment would be in the best interests of members for a number of reasons. In reality this would tend to be a good point for members to re-evaluate the adequacy (or otherwise) of their insurance arrangements particularly as they move to a new position with alternate remuneration arrangements as well as acting as an opportunity to minimise duplication of superannuation providers. The problem faced in this regard is that in respect of casual and short term contract staff the trigger points would need to be carefully considered as in many instances members could well be obtaining multiple communications and may be employed with multiple employers concurrently as well as the prospect of delays of up to 3 months in the receipt of employer SG contributions triggering the creation of accounts. Ideally changing the ATO "Tax file declaration" form on the commencement of employment to require as a mandatory field a member to confirm their superannuation provider (or authorise consolidation from a prior arrangement into an employer's new default provider via ticking a box) would go a significant way to enabling the consolidation of superannuation at the commencement of employment and avoiding duplication without creating significant administrative processes for Funds and members. Furthermore the utilisation of electronic ATO declaration forms would facilitate a smoother and less cumbersome operating model for all employers.

41. Single Touch payroll could be used to provide a more streamlined approach to consolidation. Ideally as described above making certain fields mandatory for the completion of a member (as described in 40 above) would put the onus on the member to prevent the creation of multiple accounts and could be used via single touch payroll integration as a way to avoid the unnecessary creation of duplicate superannuation accounts.

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42. Ideally the MyGov site could be expanded to capture insurance related data from superannuation providers and be a means to give the member a consolidated view and offer the opportunity to facilitate consolidation both for superannuation accounts and insurance arrangements using defined protocols across providers and with appropriate limitations to avoid over-insurance (with the consequent longer term impact to claims experience more generally).

43. Apart from what has been discussed in 40 (above) no further initiative have been identified at this time.

44. ATO reporting of multiple accounts to members could be useful as a means to facilitate consolidation however the development of insurance consolidation protocols across the industry would aid in preventing impediments where members may actively seek to maintain multiple accounts (and insurance cover) due to a fear that consolidation of cover may result in a member being unable to receive the same level of cover (or the same premium) with potential gaps due to a deterioration of health.

45. ATO reporting and the inclusion of specific questions within the tax return with data extracted and consolidated could permit members an opportunity to identify their chosen Fund for new contributions and facilitate consolidation of superannuation and insurance arrangements (based on established protocols) via the inclusion of additional relevant questions in their tax return.

46. Protocols should be established around how the cover and cost is disclosed to members and the impacts of transition of insurance arrangements so members can make an informed decision around consolidating both their account balances and insurance cover as appropriate.

C.3

47. The current regulatory environment is not supportive of consolidation in the following ways.
    a. The SG contributions are misaligned with the actual periods a member has been in employment
    b. Choice of Fund requirements place unnecessary impediments to consolidation as an employer may only institute a change in provider at annual intervals
    c. Members are not being given the opportunities at the right touchpoints to avoid the creation of duplicate accounts at the commencement of employment and through annual ATO tax return data collection (and actioning) opportunities.

48. Expanding the nature and content of insurance needs calculators which facilitate more detailed comparison based on specific terms and individual product offerings and instituting industry wide insurance transfer protocols may yield a more member centric outcome that facilitates greater consolidation.

General Questions

49. A focus should be removed from the concentration on individual benefit designs particularly in respect of benefits which would be deemed to be tailored to satisfy the common good. Solutions should be tailored to minimise or reduce the touch points that lead to the creation of multiple accounts at first instance principally as a result of the lack of minimum data requirements where opportunities exist. Taking this approach would see a significant reduction both initially and in the long term in the duplication of superannuation accounts and the creation of unnecessary insurance. It is in the interests of members and the industry as a whole that a view is not taken to address the key concerns of duplicate account through the simplistic approach that tailors solutions only to benefit designs with the potential for serious member repercussions that may not have been adequately contemplated.

50. No other solutions have been identified at this time.

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51. For the reasons outlined in 49 the key issues raised should be addressed though processes and administrative solutions that avoid the creation of unnecessary superannuation accounts at first instance rather than being prescriptive on Trustees to adopt a benefit design that is not considered appropriate to the nature, demographics and best interests of its members. As illustrated in Q28, a particular approach to the instituted benefit design to limit what could be in a default offering should not be seen as the panacea for duplicate accounts and account erosion. Ultimately one must focus on the wider issue of the potential for excessive default insurance more generally that occurs through members having multiple accounts with the consequent impact this has had on the industry as a whole through claims experience in recent years. In reality only a proportion of members would claim on cover so focusing on benefit design structure rather than administrative process and regulatory support that prevent duplicate accounts at the outset may not provide the ideal outcome for members.

52. Depending on the solution implemented, should this impact on the benefit designs of Funds transition should be based on the end of any contracted rate guarantee given the wider implication to the membership of changes that impact on the underlying claims vs premium experience for the membership pool. Administrative and supportive regulatory efficiencies to support consolidation should be implemented to support this change in approach within the industry.

53. HESTA is committed to a benefit design that addresses the needs of its members and is focused on the social good of promoting members contributing to the workforce through a return to paid employment with the aid and support of rehabilitation wherever possible. This approach is also in the national interest as it seeks to support members both contributing to society and is very reflective of an ethos that acknowledges the important and fundamental alignment of its insurance strategy with significant role our members play in the fabric of society. For this reason HESTA is committed to a long term income protection insurance design that is supportive of our members as a whole and is tailored in its design to protect our members' best interests. For this reason, we are of the firm view the issues of erosion may not simply be addressed through a fundamental shift in benefit design thinking but rather through processes aided by improvements and supported by technological solutions and disclosure (by both funds and ATO) that address the broad issues of the creation of duplicate accounts at inception rather than an approach that arbitrarily imposes a benefit design solution which could have wider implications particularly in respect of Lump Sum TPD which is seen to entrench disability.

54. We believe this question has been answered in 53 (above)

Please do not hesitate to contact Kelly Smith (ksmith@hesta.com.au) or Michael Englezakis (menglezakis@hesta.com.au).

Kind regards

Kelly Smith

General Manager, Administration and Insurance

HESTA

Cc: Mary Delahunty, Stephen Reilly, David Haynes

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