asfa
the voice of super

SUBMISSION

Submission to the Senate Economics Legislation Committee — *Treasury Laws Amendment (Putting Members' Interests First) Bill 2019*

15 July 2019

The Association of Superannuation Funds of Australia Limited
Level 11, 77 Castlereagh Street
Sydney NSW 2000

PO Box 1485
Sydney NSW 2001

T +61 2 9264 9300
1800 812 798 (outside Sydney)
F 1300 926 484
W www.superannuation.asn.au

ABN 29 002 786 290 CAN 002 786 290

File Name: 2019/15

15 July 2019

Committee Secretary

Senate Economics Legislation Committee

PO Box 6100

Parliament House

Canberra ACT 2600

Via email to: economics.sen@aph.gov.au

Dear Committee Secretary

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

The Association of Superannuation Funds of Australia (ASFA) is pleased to provide this response to the Committee's inquiry into the *Treasury Laws Amendment (Putting Members' Interests First) Bill 2019* (the Bill).

ASFA is a non-profit, non-political national organisation whose mission is to continuously improve the superannuation system, so all Australians can enjoy a comfortable and dignified retirement. We focus on the issues that affect the entire Australian superannuation system and its $2.7 trillion in retirement savings. Our membership is across all parts of the industry, including corporate, public sector, industry and retail superannuation funds, and associated service providers, representing over 90 per cent of the 14.8 million Australians with superannuation.

If you have any queries or comments in relation to our submission, please contact me on (02) 8079 0805 or mfahy@superannuation.asn.au, or Byron Addison, Senior Policy Advisor, on (02) 8079 0834 or baddison@superannuation.asn.au.

Yours sincerely

Martin Fahy
Chief Executive Officer

*****

General comments

Treasury Laws Amendment (Putting Members' Interests First) Bill 2019 **(the PMIF Bill)**

ASFA supports policy initiatives that improve the Australian superannuation system. In particular those initiatives that protect people with low balance accounts, younger members and those who are on low incomes. In this context, default insurance in superannuation should be appropriate to the needs of different member cohorts.

We recognise the aim of the draft Bill to prevent the erosion of accounts through unnecessary insurance premiums but we consider that the proposed measures could be better targeted to prevent people losing insurance that will protect them and their families in the event of injury, illness leading to temporary or permanent incapacity or death.

This is especially the case for those employed in high risk or hazardous occupations – police officers, paramedics and other emergency services workers, miners, and building and construction workers. These are people whose work exposes them to a significantly higher risk of injury or death than the rest of the community and who for this reason find it hard to obtain insurance at reasonable rates outside of group insurance in superannuation, if at all.

These changes will take time to implement and our members have questioned the feasibility of a 1 October 2019 start date, especially as this start date includes a requirement to notify affected members about the changes by 1 August 2019. The industry has already devoted considerable resources to implementing the *Protecting Your Super* package changes and these proposals will require further significant changes to existing contractual arrangements and insurance premiums and the need to cater to additional reporting and administrative requirements. In addition, all measures will involve substantial communication and disclosure costs and obligations.

There is also the risk that superannuation fund members are already suffering from a degree of confusion arising from the various communication campaigns used to explain the impact of the Protecting Your Super reforms and the likelihood that fund members will be resistant or unresponsive to a further campaign. There will also be an elevated volume of communications this year as the ATO consolidation transfers are processed, in addition to the usual release of annual statements, which will increase the likelihood of confusion for members.

ASFA recommends a delay in the start date for the PMIF reforms to at least 1 April 2020. This will mean that funds have a greater ability to implement the operational, communication and disclosure requirements contained in the final form of the PMIF Bill, if and when it is passed by the Parliament, and the requirements in the associated regulations.

ASFA considers that there are a significant number of people under age 25 with dependants who would benefit from insurance if the policy holder were to get injured or die. For this reason, ASFA supports making automatic or default cover opt-in to those aged under 21.

ASFA does not support the removal of automatic or default cover for members with active low balance accounts (accounts where contributions are being received). In many cases the receipt of employer contributions is likely to bring the account balance above $6,000 within a relatively short time but the timing will depend on income and work patterns and this variability will create different results for members where previously eligibility was consistent. It particularly discriminates against women who on average receive lower pay than men and are more likely to be employed on a casual basis or suffer broken work patterns.

Case study scenarios for low balance members

Carol and Janet are both 25 years of age, and both have a superannuation balance of $3,000 (while this amount is somewhat lower than the median balance for someone aged 25, it is certainly the case that a significant minority of people aged 25 would have balance around this amount).

Carol starts a new full-time job, earning $50,000 per year. Carol's account receives Superannuation Guarantee contributions, and her super balance reaches $6,000 in around **nine** months. Janet also starts a new job. Janet works part-time, earning $25,000 per year. With Superannuation Guarantee contributions, Janet's super balance reaches $6,000 in around a **year and a half**.

If instead Carol and Janet had no superannuation when they started their jobs, it would take Carol around a year and a half to reach $6,000 while it would take Janet more than two years.

Recommendation

ASFA considers that the proposed package of insurance changes should be modified as follows to achieve a better balance between providing insurance benefits and minimising the impact this has on retirement savings:

- The start date should be delayed until at least 1 April 2020 to allow fund members to be notified about the change and time to make a considered decision about their insurance needs and so that funds have time to implement the necessary system changes and update their disclosure material
- Changing the minimum age that automatic cover can be provided to new members to 21
- Allowing new contributory members over any prescribed minimum age being provided with automatic cover immediately upon joining a fund without having to accrue a $6,000 balance
- Introducing further exemptions to allow funds to provide (and continue to provide) insurance on an opt-out basis to members in higher risk occupations and to allow for risk only and certain legacy products to not be impacted to the detriment of members
- The employer sponsor contribution exception should be amended to permit the exception to apply: where the employer funds more than half of the member's insurance premiums in an employer-sponsored scheme; and where the cost of the premiums is borne by the employer without an 'amount' being paid. The quarterly notification requirement should also be amended to make it annual.

Detailed comments

1. Schedule 1: Low-balance accounts and members under 25

1.1 No insurance provided to superannuation fund members with a low balance account

ASFA supports insurance being ceased on accounts that are susceptible to extreme and unnecessary benefit erosion. The Explanatory Memorandum released with the Bill indicates that Treasury has estimated that approximately 6 million accounts are below $6,000 and have not received an amount in the last 13 months. Ceasing any insurance cover for these members makes sense if they have not provided a confirmation that they wish to retain it. The majority of perverse outcomes that result from unnecessary premiums being charged to accounts are from this cohort.

The inactivity test introduced under the *Protecting Your Super* package (no contributions for 16 months) will remove insurance for this cohort unless members make an election to retain it. **This means that the low balance measure in the PMIF Bill will apply principally to members with active accounts.**

As we have outlined in previous submissions ASFA supports inactive accounts below $6,000 having all insurances ceased (unless members have consented to retain it). This would have been an appropriate and sensible targeted measure and aligned with the stated objective of the reforms being to "limit the erosion of retirement balances for younger and low balance account holders".

However, ASFA does not support ceasing insurance for existing fund members that have an account balance below $6,000 that is receiving contributions. Similarly, new members should not have to wait until an account balance builds up to $6,000 before insurance is provided to them on an opt-out basis.

In terms of cost, the average cost for default life insurance in superannuation has been estimated to be $3 per week and half that amount for younger members.[1] When this average is considered against average weekly earnings rates for all employees of $1,191.70, premiums are affordable in the context of 9.5% super guarantee contributions being made for employees and good value for the level and nature of the cover provided.

Delaying the allocation of an opt-out insurance policy to a superannuation account until it builds up to over $6,000 will create a series of unnecessary administration and insurance risk management issues. Anti-selection is common when insurance is voluntary as opposed to default because generally higher risk members will opt-in and lower risk members will not. This will add to the pressure on the prices members will have to pay for insurance in super. Additionally, members will not have cover for varying periods and in some cases quite lengthy timeframes after they join a superannuation fund depending on their work patterns.

1.2 No automatic insurance for new superannuation fund members under the age of 25

ASFA maintains that if there is to be an age based restriction on providing default insurance in superannuation on an opt-out basis, then age 21 is most appropriate. This will minimise the unintended consequence of these changes and reflect the fact that 21 is the age by which many Australians have commenced full-time employment. According to ABS statistics, 40 per cent of employees under 25 are working on a full time basis – approximately 585,000 individuals.

Evidence relating to the insurance needs that this cohort has and the rate of claims that have been paid to these members is compelling.

We outlined in a previous submission to Treasury that in 2015-16 there were nearly 300,000 households in Australia containing around 450,000 employed persons with the household head less than 25 years of age. There were nearly 60,000 dependent children in such households and in around 100,000 homes the household head had a spouse.[2]

Additionally, an ASFA superannuation fund member has provided us with information on the frequency of claims paid to younger members. This fund, over the last 16 years has paid 1,036 insurance claims to those under 25 - 733 death benefits totalling $94.4 million and 303 TPD benefits totalling $23 million. For the death benefit claims, for those aged between 21 and 25, approximately 60 per cent of payments went to dependants. An ASFA insurer member has also indicated that the rates of disability claims are the same for people aged 20 and those aged 30.

ASFA notes that AIA, a leading insurer, commissioned Rice Warner to undertake research on the impacts of the Government's reforms and proposed PMIF reforms.[3] This research considered the longer term impacts on individuals' retirement balances in the scenario of opt-out insurance being deferred until age 25. It concluded that when premium rates did not change as a result of the reforms, a marginal 0.76 per cent improvement in retirement balance would arise. In the more likely situation, when insurance premiums increase due to changed risk pooling, this improvement reduces or is even reversed depending on the size of the premium increase. With a 15 per cent increase, as estimated by Rice Warner, the improvement becomes 0.27 per cent only. In similar research undertaken by KPMG[4], the projected premium increase is 26 per cent and at these levels the percentage impact on retirement balances becomes detrimental against current settings.

[1] Rainmaker June 2018

[2] ABS – Household Income and Wealth survey 2015-16

[3] Rice Warner – Economic Impact of 2018 Federal Budget Proposed Insurance Changes (May 2018).

[4] KPMG – The impacts and unintended consequences of the proposed Federal Budget changes (June 2018).

1.3 Timing

The PMIF measures will have a significant impact on fund administration and operations. Amongst other things, fund disclosure documents will need to be updated, and affected members identified and notified. Fund members also require a reasonable period to consider their insurance needs and to determine whether their insurance should be maintained.

ASFA considers that the timetable in the Bill does not provide enough time for these activities to be completed or for fund members to digest the changes and make a considered decision. We seek an extension until at least 1 April 2020 to enable the industry to implement the changes and notify members in a timely fashion. A three month delay would require notifications to be sent out in the lead up to Christmas and cancellations to occur in the Christmas holiday period which would be a poor outcome for members. In this period there will already be ATO consolidation and receiving fund notices plus annual statements as well as ongoing inactivity notices (see 1.9).

Funds will also need time to renegotiate their contractual arrangements with their insurers to reflect the PMIF changes and this could not be done by the 1 October deadline.

In addition to targeted fund campaigns, the industry ran a public awareness campaign to explain the Protecting Your Super changes and it may be appropriate to run a similar campaign for the PMIF changes to ensure the changes are explained and to give fund members the time and opportunity to make an informed decision about their insurance needs. However this would be challenging given the existing timetable in the PMIF Bill and a delayed start date would support the effectiveness of such a campaign.

ASFA notes that in the lead up to 1 July which was the start date for the Protecting Your Super insurance measures many fund's contact centres were overwhelmed by member enquiries despite additional resources being assigned to them. A delay in the start date for PMIF would allow the industry to make a proper assessment of their Protecting Your Super implementation and communication campaigns and identify what worked and what didn't. A delay would also give funds more time to target or stagger communications to members to smooth the likely response rate and lessen the burden placed on contact centres. This would help to ensure that any member who needs further information about the PMIF measures is able to obtain it efficiently before the cancellation date to be able to make an informed decision.

Summary example of PMIF implementation project requirements

- Registry changes will be required to support opt-In for under 25s and low balance accounts. This would include the full IT development of Design, Build, Test etc.
- Super employer and member website access changes – new member web pages will be required

- Changes to disclosure / Welcome packs by the start date for new default members
- Significant Event Notices (SEN) will need to be sent to existing members
- PDSs and web disclosure information will need to be updated plus updates to forms/templates
- New insurance internet pages will be required to capture details to support the age 25 opt-in
- Member communications will need to be drafted and put through internal sign off including marketing, legal and compliance, member services
- Mailhouse/electronic communications providers to be notified and projects commenced
- Insurance contract with providers will need to be re-negotiated.

It should be noted that it is difficult for funds to prepare for measures such as the PMIF ones and impossible without the regulations being made and that should also form part of any consideration given towards selecting an appropriate start date.

1.4 Exception for high risk occupations – Police, Emergency services, miners and construction workers

ASFA considers that exemptions should be included to allow those employed in higher risk occupations to retain access to the current opt-out framework in the same way as those employed in the Defence Force are exempted from the PMIF and the *Protecting Your Super* measures.

ATO figures[5] show that in 2015-16 the Australian workforce consisted of over: 59,000 police officers; 50,000 miners; 15,000 ambulance officers/paramedics; and 14,000 air transport professionals. All of these individuals and many of the potentially hundreds of thousands from a range of building and construction sectors would have challenges getting insurance if it were not for current settings.

1.5 Risk only products exemption

Risk only superannuation products should be given an exemption from the low balance measure. Risk only products have a nil balance and therefore are not exposed to the risk of balance erosion. Further, risk only products are not allocated on an opt-out basis but rather insurance can only be provided by member election.

1.6 Legacy product exemption

There is an intention to exempt certain legacy products (fixed term and 'paid up' policies) from the *Protecting Your Super* package measures and for consistency that exemption should be extended to the PMIF low balance measure.

[5] ATO Annual Individual Income Tax Statistics – 2015/16

1.7 Amendments required for consistency with Protecting Your Super amendments

We welcome the proposed amendments to the *Protecting Your Super* package measures announced by APRA on 28 June 2019 that will address the aggregation of a member's interests in one or more products and the rights of members under fixed term insurance so that cover is not inappropriately removed. ASFA recommends that these amendments be extended to the PMIF measures for consistency and to ensure that the unintended consequences of the Protecting Your Super package are also avoided in PMIF.

Ideally these amendments should be made available for consultation before any consideration of the PMIF Bill so that the Bill can be considered in its final form.

1.8 Elections made under the Protecting Your Super package measures should extend to PMIF and should remain valid through a Successor Fund Transfer

ASFA considers that any election made in response to the *Protecting Your Super* package insurance inactivity test (S.68AAA (2)) should also be valid for the low balance test and a reference to this be added to the PMIF Bill. It is confusing for members to have to make more than one election to maintain their insurance and there is the risk that members will ignore a second election notice, confident that they have already completed this task.

Example

John has an inactive low balance account because he wished to maintain his insurance policy after leaving his previous employer. He received a notice in May 2019 advising him that his account had been inactive for 16 months and that unless he made an election the cover would be cancelled 1 July 2019. John made an election via SMS and because he was worried that he might lose the insurance he made an election on the fund's website also. (There is anecdotal evidence that many members who wished to maintain their insurance made multiple attempts to do so).

As a result of PMIF John receives a subsequent notice advising him that his cover is about to be cancelled because it is low balance. John ignores the second notice thinking that it must be a duplicate having made an election only a few months beforehand.

ASFA also considers that elections made in a fund where there is a successor fund transfer (SFT), or a trustee initiated intra-fund transfer between products in the same fund, should be permitted to be carried over to the new fund or product, to minimise the possibility of members who have opted-in from unintentionally losing their insurance entitlement.

Members who apply for insurance cover post the stocktake date (currently set at 1 July) should be considered to have made an election for the purposes of 68AAB(2). Based on the current drafting of the legislation and the relevant applicable timeframes, these members will be required to be provided a notification and make an additional election. The legislation should be amended to enable members who apply for cover, or make a 'positive act', after the stocktake date but before the start date (currently set at 1 October 2019), to be treated as having made an election for the purposes of s68AAB.

1.9 Overlapping inactivity notifications and notifications required to low balance account members

Due to the existing requirements implemented under the Protecting Your Super changes, Trustees are required to issue inactivity notifications to members once their account becomes inactive 7, 4 and 1 month prior to the inactivity period. This means some members may receive, or may have already received, an inactivity notice in addition to requiring a notice to be sent to them under the PMIF Bill if their account balance is also less than $6,000 as at the stocktake date.

This is an unintended consequence which will confuse members, and may cause notifications to be misleading.

Transition provisions should exclude individuals who have already been provided an inactivity notice from the low balance provisions, to prevent insurance cancellations already notified from being effectively brought forward.

Communication overlap example

Kate has a low balance account and has received an insurance inactivity notice (PYS) telling her that her account has been inactive for 9 months (her fund's period of inactivity is 16 months) and that if she doesn't make an election or a contribution is not made her insurance will lapse in 7 months' time.

Kate a month later receives a PMIF notice telling her that her insurance will lapse in 2 months' time because it is low balance unless she makes an election.

1.10 Employer sponsor contribution exception

ASFA welcomed the addition of the employer-sponsor contribution exception defined at S. 68AAE of the *Superannuation Industry (Supervision Act) 1993*. However to maintain valuable and tailored insurance for employees who are members of these schemes we consider that the requirements to qualify for the exception should be relaxed to permit the exception to apply where the employer funds a high proportion of the insurance cost but not the full amount. For example, an employer-sponsored scheme may include a small compulsory member contribution to partially defray the cost of income protection premiums.

ASFA recommends that S.68AAE subsection (e) be amended to permit the exception to apply where the proportion of the premiums paid by the employer is higher than a percentage threshold rather than the existing requirement for it to be ‘equal to or greater than the insurance fees’. 50% or more than half would appear to be a reasonable threshold as account erosion is unlikely to occur in this circumstance and is therefore consistent with the policy intent of the *Protecting Your Super* and PMIF measures.

In some cases, where a fund runs both defined benefit and defined contribution schemes, the employer covers the cost of insurance from an employer reserve but does not strictly contribute ‘amounts’ to the fund. It would be desirable if subsection (d) were amended to reflect the fact that the cost is **borne** by the employer rather than the **amount** the employer contributes to recognise different funding mechanisms and to maintain cover that is tailored to the needs of employees.

The requirements for the employer exception also create undue administrative burden. This could be addressed by amending the legislation to allow employers to provide notices annually (rather than quarterly) and to allow a single notice to be provided in respect of all existing and future members of an employer plan.

1.11 Notification of elections to maintain insurance

The PMIF Bill requires members to make an election to maintain insurance in writing (Subsections 68AAB (2) and 68AAC (2) while the Explanatory Memorandum (1.37 to 1.40) suggests that the election can be made in a variety of ways including a note following a telephone conversation. These subsections should be amended to make it clear that ‘in writing’ includes a note recording the election made by an adviser or fund representative or the record of an instruction given to a contact centre representative.

2. Technical amendments

2.1 Members with active or pending claims

ASFA considers that the PMIF and Protecting Your Super reforms should provide protection for members who are receiving insurance benefits or waiting for a claim to be assessed. While cancelling insurance due to inactivity or low balance is unlikely to have an impact on the claim itself, it may affect the member's ability to make further claims (eg it is not uncommon for a member receiving Salary Continuance insurance payments to later make a TPD claim or face a higher likelihood of death).

ASFA recommends that the Bill is amended to ensure that insurance is not required to be cancelled if a member is receiving insurance benefits or has a pending claim.

2.2 Uncontactable members

The Corporations Regulations provide exemptions for communications relating to accounts, including the issuing of periodic statements, where the trustee has no address or has an incorrect address for the member and after making reasonable attempts has been unable to contact the member. No similar exemption exists for notices relating to the Protecting Your Super or PMIF notices and a similar exemption for these notices would be appropriate.

We recommend that the application provisions for proposed section 68AAB of the SIS Act be amended as well as regulations 7.9.44B and 7.9.44C of the Corporations Regulation to include provisions similar to those that currently exist in relation to notification of material changes or significant events (Subsections 1017B(7A), (7B) and (7C) of the Corporations Act, as amended by Schedule 10A of the Corporations Regulations) and periodic statements (Subsections 1017D(8), (9) and (10) of the Corporations Act, as amended by Schedule 10A of the Corporations Regulations).

2.3 Notifications required to be issued to new members who join from the stocktake date (currently set at 1 July)

Based on the PMIF Bill as currently drafted, notifications are required to be provided to all members who begin to hold a product between the stocktake date and the start date that their insurance will be cancelled on the start date unless their balance reaches $6,000 or they make an election. These notifications are required to be sent to members regardless of whether or not they have elected to take out insurance upon joining. These members should not have to make a further election.

2.4 Notifications to members who join after the stocktake date (currently set at 1 July 2019)

There is no timeframe provided by which trustees must issue notifications to members that join from the stocktake date. It is not feasible for trustees to write to new members who join in the few weeks or days prior to the start date (currently set at 1 October) to notify them about their insurance prior to the start date.

The transitional communication requirements should be amended to simplify member experience. An alternative approach would be to allow insurance for these members to continue for a further two months (currently until 1 December 2019) to allow funds to adequately communicate to these members and provide them with time to consider their circumstance and make an election.