

SUBMISSION

Submission to APRA — Proposed revisions to Prudential Standard SPS 250 Insurance in Superannuation

3 February 2020

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Proposed revisions to Prudential Standard SPS 250 Insurance in Superannuation

The Association of Superannuation Funds of Australia (ASFA) is writing to you in response to APRA's consultation on the proposed revisions to Prudential Standard SPS 250 Insurance in Superannuation.

About ASFA

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 \$2.9 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 16 million Australians with superannuation.

General comments

ASFA is responding to this consultation both as an industry association representing our members and also as a Code owner of the Insurance in Superannuation Voluntary Code of Practice (the Code).

ASFA supports the role of insurance in superannuation and considers that it provides significant benefits to superannuation fund members. We also support measures that enhance the operation of insurance in superannuation so that its benefits are delivered to members as efficiently as possible.

In general terms we support the areas APRA has chosen to target in its proposed revisions to SPS 250, namely the inappropriate erosion of accounts, appropriate occupational defaults, the ease of opting out of insurance, and a robust framework for related party appointments. However in some cases it is not clear how these measures are to be applied by trustees in practice and in the absence of formal prudential guidance our members seek clarification of APRA's expectations and more detailed direction for their implementation.

Independent certification for insurance arrangements with related parties or where priority or privilege has been given to an insurer – ASFA members are broadly supportive of this measure but would appreciate further clarity about what the various elements will mean in practice. It would be beneficial if the further guidance could be provided about the definitions of independence, priority and privilege as well as how the best interests of beneficiaries is to be determined in this context.

Inappropriate erosion of retirement income - ASFA considers that it is important, in working towards a framework for how inappropriate erosion is to be determined, that trustees be given a degree of flexibility to allow them to maintain member benefits where it is appropriate to do so.

Affordability of insurance was one of the areas which attracted a lot of attention during the development of the Code and one of the measures adopted to address this was a limitation for members who receive insurance automatically that premiums not exceed 1 per cent of an estimated level of salary for the membership generally, or segments of that membership.

However we would emphasise that this was always intended to be confined to members who receive insurance automatically and it was also deliberately intended to be applied on 'if not, why not' basis. This was because some trustees with members in certain scenarios such as employment in high risk occupations, or who have determined that income protection should be offered as a default to meet the needs of their membership, could not meet the 1 per cent limit without substantially reducing the insurance benefits provided to their members. These trustees felt this would be against their members' best interest and potentially a breach of their fiduciary obligations.

SPS 250 and the Code - ASFA as a Code owner is also conscious that there is a degree of overlap between the inappropriate erosion and occupational default measures and the Code. ASFA, along with the other Code owners, has been reviewing the Code in light of the changes brought about by the Protecting Your Super (PYS) and Putting Members' Interests' First (PMIF) packages and in doing so has determined that the Code should not attempt to duplicate standards which are enforced through legislation or other instruments. This principle may also apply to those areas where SPS 250 will overlap with the Code and ASFA would be keen to discuss with APRA how SPS 250 and the Code should interact in future.

Finally, it should be noted that recent legislative reforms also relate to some of the proposed revisions, in particular that relating to inappropriate erosion. While ASFA expressed certain reservations about aspects of the PYS and PMIF reforms there is no question that they will do much to reduce the impact of insurance premiums on low balance accounts in particular but also high balance inactive accounts and minimise the number of duplicate accounts. The new member outcomes requirements and especially the annual members outcomes assessment also require trustees to assess whether insurance fees inappropriately erode retirement income and it would be beneficial to understand better how APRA intends the measures in SPS 250 to operate in harmony with these legislative reforms.

Specific comments

Timing

A number of ASFA members have suggested that due to the connections between the proposed revisions to SPS 250 and the Code that it would be better for the commencement date of the measures be delayed to 30 June 2021 to match the Code's final compliance date.

A process that enables beneficiaries to easily opt out of insurance cover

ASFA members support the requirement to make it easy for members to cancel their cover however they would like greater clarity about the criteria that would be required for a trustee to satisfy itself that the process it offers meets this obligation.

Clause 12(f) aligns with the Code's requirement for 'cancelling your insurance cover' in section 4.18 of the Code.

Section 4.18 provides that a member can cancel or reduce their cover, subject to appropriate member identification:

- a) via the fund website, the insurer's website or another fund digital application;
- b) over the phone; or
- c) in writing by email or post.

Sections 4.19 to 4.22 also specify other requirements relating to the cancellation of cover including the requirement to refund premiums if the cover is cancelled within 14 days of the member receiving notification of the cover's commencement.

ASFA seeks guidance as to whether compliance with these sections of the Code would satisfy APRA's expectations for best practice or whether other or additional best practice criteria should apply. If further or different criteria will apply the Code owners would need to consider amending the Code to prevent duplication or inconsistency with the prudential standard.

ASFA seeks further guidance on the criteria for trustees to implement a process to provide ease of opting out of insurance cover.

ASFA notes the interaction of the new requirement and the Code and the potential need for the Code to be amended.

How a trustee is to determine that the level and type of cover does not inappropriately erode the retirement income of beneficiaries

This new requirement is linked to the Member Outcomes assessment, the annual business performance review requirement in SPS 515 and SPG 516, the existing insurance covenant (specifically S.52(7) of the SIS Act) and the sections of the Code that relate to appropriate and affordable cover.

ASFA seeks further clarity from APRA about how this new requirement is meant to connect with the Member Outcomes requirements and how it relates to the Code.

The Code contains a number of benefit design requirements to ensure that insurance cover provided to members is appropriate and affordable. In particular there is a requirement that premiums for automatic insurance members are not to exceed 1 per cent of an estimated level of salary for the membership generally. This 1 per cent limit was never intended to apply to members who had taken out voluntary cover or had ceased to be regarded as automatic insurance members. In recognition of the fact that some trustees would not be able to meet this limit, due to having members in high risk occupations or with other particular characteristics such as needing to have income protection provided automatically, the Code permitted trustees to exceed the 1 per cent limit as long as they documented and published the rationale for doing so.

Some ASFA members are concerned that the 1 per cent limit in the Code may be used as a criterion under this test and that the flexibility deliberately provided under the Code may be reduced or lost. There is also concern that it might be applied to voluntary cover or other types of cover not provided automatically, for example where a member has elected to increase or reactivate their cover beyond the default limits after a 'life event' such as turning 30.

Some ASFA members have questioned the use of the word 'confirmed' in clause 16 (a). This can be regarded as setting too high a bar and may be difficult to achieve in practice. A possible alternative would be to replace 'confirmed' with 'assessed'.

It would also be useful if APRA could confirm whether it is acceptable for trustees to use the results of their member outcomes assessments and business performance reviews to determine that the level and type of cover will not inappropriately erode the retirement income of beneficiaries.

It should be noted that the PYS and PMIF reforms have put pressure on insurance premiums due to a reduction in the size of the insurance pool and because they have introduced uncertainty about future opt-in and claims rates and this pressure may continue for some time.

The PYS and PMIF reforms have also imposed benefit design changes on insurance cover in superannuation that relate directly to where affordability/inappropriate erosion are likely to be most relevant.

ASFA seeks further guidance on APRA's expectations for determining inappropriate erosion.

ASFA cautions against the use of fixed thresholds in making this determination as they would not take into account of differing circumstances such as a trustee's membership profile.

Any status attributed to a beneficiary (including a class or cohort of beneficiaries) in connection with the provision of insurance must be fair and reasonable

ASFA supports this proposal in principle, which is intended to address recommendation 4.15 from the Royal Commission. However additional guidance would be welcome from APRA:

- confirming that a 'status' in this context would be any that affects the premium charged, including smoker status or occupation rating
- specifying the factors a trustee should consider in determining whether a status attribution is 'fair and reasonable'.

For example, one ASFA member classifies their insured members into five categories. These categories include high risk, heavy manual, light manual, white collar and professional. Their current default insurance arrangement defaults members into the high-risk category because data indicates that a majority of the membership works in that category. When a new member joins the fund, they seek to confirm their job classification for insurance purposes as part of the welcome telephone call process but if there is no response they use the high risk category as the default.

It should also be noted that this requirement overlaps with section 4.13 of the Code which we will need to consider reviewing to prevent duplication.

ASFA seeks further guidance on what constitutes 'fair and reasonable' for status attributions.

ASFA notes that the Code will need to be amended once further guidance is provided.

New independent certification requirements

ASFA supports a robust framework for all related party appointments however we seek further guidance on a number of elements in clauses 24 and 25.

Priority/privilege

It would be beneficial if APRA provided further detail about what scenarios it envisages amounting to the giving of priority or privilege to an insurer. For example, trustees may undertake a 'closed tender' for insurance services or they may draw an insurer from a pre-approved panel of insurers selected for tailored insurance arrangements in employer plans. ASFA does not consider that these examples should be regarded as the giving of priority or privilege, but further guidance is sought to clarify this.

In terms of priority or privilege, some ASFA members have suggested that exclusivity clauses, arrangement duration, target loss ratios and rate review triggers could be regarded as examples of insurance arrangements that may give 'priority or privilege' to an insurer.

Independent certification

ASFA supports this proposed requirement in general terms but there are a number of areas where guidance would be beneficial. These can be broadly categorised under the following headings: party performing the certification; and the certification criteria and requirements.

Party performing the certification

- What qualifications are required for a party to be able to provide certification on these matters?
- What type of company or professional does APRA see as suitable to perform this certification?
- Will APRA maintain a register of qualified entities or professionals?
- What are APRA's expectations in the event that a Trustee is unable to secure a suitability qualified independent party to perform the certification?

Certification criteria and requirements

- What information must be provided in the certification?
- What criteria or principles must be assessed as part of the certification process?
- How is 'best interests' required to be interpreted in this context?
- Is it appropriate for a trustee to outsource the determination of whether an insurance arrangement is in the best interests of beneficiaries to a third party given this is ultimately a trustee responsibility?
- Is there an expectation that the certification will be a legal opinion?

It is important that APRA's expectations for these issues be clearly defined to ensure consistency across all independent certifications.

With regard to existing insurance arrangements, we would appreciate it if APRA could clarify whether the proposed requirements apply from the earlier of:

- renewal of an existing insurance arrangement after 1 January 2021
- 1 January 2023 (2 years from 1 January 2021)

Some ASFA members would also appreciate further guidance on whether the requirements apply to closed insurance products.

ASFA seeks further guidance on the requirements for independent certification, the determination of best interests for beneficiaries and the definition of priority and privilege in relation to insurer appointments.

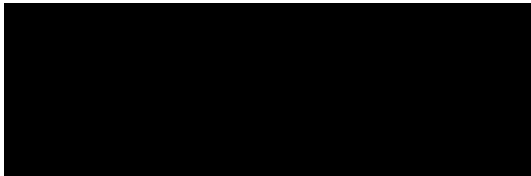
An insurance arrangement must give an RSE licensee the right to terminate the arrangement, should the independent certification be negative

From a practical perspective ASFA would appreciate APRA's guidance on the steps it expects trustees to take in the transition period to ensure that members covered by an arrangement that has been terminated are not left worse off.

As described above further clarity is sought as to what a 'negative' assessment might mean in practice. It is clear that a negative assessment would mean a certification that finds that an insurance arrangement is not in the best interests of its beneficiaries or does not satisfy all applicable legal and regulatory requirements but it would be desirable if further guidance could be provided as to how best interests are to be determined and specifically what legal and regulatory requirements are relevant.



Yours sincerely



Chief Policy Officer and Deputy CEO