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18 February 2014

**Subject:** Consultation on proposed Modification Declaration – Superannuation Industry (Supervision) Regulations 1994, r. 4.07E(8)

Dear Sir/Madam

We appreciate:

- APRA's early action to correct what appears to be an unintended outcome of Regulation 4.07E; and
- The opportunity to comment on the draft Modification Declaration.

We note a number of concerns with the draft:

1. It appears to cover situations where there has been only one successor fund transfer. Further modifications are necessary to allow for a series of successor fund transfers.
2. The ability to continue self-insuring in a successor fund is limited to defined benefit members who had self-insurance in the original fund. Self-insurance is not possible for new defined benefit members or for defined benefit members who were not self-insured, or not self-insured for the particular risk (perhaps because they were in a different category of the transferring fund). (This is inconsistent with the provisions applicable to an ongoing fund where there has been no successor fund transfer. In such a case, self-insurance can also apply to new defined benefit members and defined benefit members who were previously not self-insured.) The Modification Declaration needs to be amended to allow rules consistent with the provisions for an ongoing fund (Refer to note below).

3. It does not enable self-insurance to be continued in a fund which does not satisfy the definition of successor fund even though the defined benefits are not changing (for example, arrangements for the non-defined benefit component of a member's benefit may be changing (such as higher fees) making it impossible for a successor fund transfer to occur – even though there may be no changes to the defined benefit arrangements). More flexibility to cover such non-successor fund transfers should be provided or is it intended such cases could be allowed via specific APRA approval on application?
4. It does not address concerns with Reg 4.07E(8) which appears to stop a fund from self-insuring defined benefit members from 1 July 2016 if the RSE licensee previously had a condition prohibiting self-insurance for defined benefit members but the condition had been removed before 1 July 2013 and self-insurance was in place at 1 July 2013.
5. It does not address concerns with Reg 4.07E(8) which might be interpreted in a way which prevents self-insurance for defined benefit members in Fund A which self-insured such members at 1 July 2013 where the RSE Licensee was prohibited (due to a condition on its licence) from providing self-insurance for defined benefit members in relation to a different fund, Fund B.

Note: If self-insurance is not allowed for new members or for existing transferred members who subsequently transfer from a non-self-insured category to a self-insured category, numerous problems will arise:

- It may be necessary to obtain insurance for a very small number of members (new members or transfers). In view of the small number of insured members, a viable group insurance policy (with or without any automatic acceptance provisions) may not be available. In any case, such insurance may be subject to underwriting conditions resulting in some members being uninsurable or subject to limited cover
- Defined benefit funds may provide benefits which are uninsurable. Hence, it may be necessary to amend the benefit design for new members and members transferring between categories to remove any uninsurable benefits which are currently self-insured. In some cases, the amendments to the benefit design that would effectively be required by the Modification Declaration may prevent a successor fund transfer or force the trustee to reduce existing rights (for members who transfer categories after the SFT and cannot be provided with self-insured benefits). This is not in the best interests of members.

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- Costs will increase due to mixture of self-insurance and insurance for defined benefit members. It will be necessary to establish different procedures in relation to each. Member communication will be more difficult with potentially different rules and processes applying to defined benefit members depending on when they joined the fund or transferred to their relevant benefit category.

Unless the appropriate modifications are made, the restrictions on self-insurance will result in increased red-tape, higher costs and a potential reduction in members' rights and benefits. It will also act as a barrier to fund rationalisation. We cannot see that this would be justifiable given that the restrictions would not apply if the SFT was abandoned and the original fund continued on, or if the SFT proceeded but the self-insuring fund became the on-going fund.

Please contact John Ward (03 9623 5552) if you have any queries on our submission.

Yours sincerely,



Dr David Knox  
Senior Partner