

EXPLANATORY MEMORANDUM (EXPOSURE DRAFT)

Minute No. of 2012 - Minister for Financial Services and Superannuation

Subject - *Corporations Act 2001*

Superannuation Guarantee (Administration) Act 1992

Superannuation Industry (Supervision) Act 1993

Superannuation Legislation Amendment Regulation 2012 (No.)

Subsection 1364(1) of the *Corporations Act 2001* (the Corporations Act) provides, in part, that the Governor-General may make regulations prescribing all matters required or permitted by the Corporations Act to be prescribed, or necessary or convenient to be prescribed for carrying out or giving effect to the Corporations Act. The *Corporations Regulations 2001* (the Corporations Regulations) are made under section 1364 of the Corporations Act.

Section 80 of the *Superannuation Guarantee (Administration) Act 1992* (the SGA Act) provides, in part, that the Governor-General may make regulations prescribing all matters required or permitted by the SGA Act to be prescribed, or necessary or convenient to be prescribed for carrying out or giving effect to the SGA Act. The *Superannuation Guarantee (Administration) Regulations 1993* (the SGA Regulations) are made under section 80 of the SGA Act.

Subsection 353(1) of the *Superannuation Industry (Supervision) Act 1993* (the SIS Act) provides, in part, that the Governor-General may make regulations prescribing matters required or permitted by the SIS Act to be prescribed, or necessary or convenient to be prescribed for carrying out or giving effect to the SIS Act. The *Superannuation Industry (Supervision) Regulations 1994* (SIS Regulations) are made under section 353 of the SIS Act.

On 16 December 2010, the Government announced Stronger Super in response to the recommendations of the Super System Review final report. Following extensive consultation, on 21 September 2011 the Government announced its decisions on key design aspects of the Stronger Super reforms.

The purpose of the proposed regulations is to give effect to changes arising from legislation implementing MySuper and governance reforms.

The proposed regulations:

- require trustees to provide a significant event notice to a member of a MySuper product, where the trustee, or an associate of the trustee, suggests or recommends to the member that they transfer their interest in the MySuper product to any other product;
- amend the conditions for insurance in respect of death that superannuation funds must meet in order for contributions to those funds to satisfy choice of fund requirements;

- allow the existing definition of permanent incapacity in the SIS Regulations to apply for the purposes of the SIS Act;
- prohibit trustees from providing insured benefits for members unless they are backed by an insurance policy from an insurer;
- prohibit trustees from providing externally insured benefits (other than those that satisfy the conditions of release in the SIS Regulations for death, terminal medical condition, permanent incapacity and temporary incapacity), to beneficiaries who join the fund from 1 July 2013;
- exempt the transfer of accrued default amounts to a MySuper product in another fund from the successor fund transfer rules;
- require trustees to provide a notice to a member when they are attributing the member's accrued default amount to a MySuper product or moving it to another fund; and
- allow life and total and permanent disability (TPD) insurance to be offered on a compulsory basis for MySuper members if the trustee is reasonably satisfied the insurance cannot be provided on an opt-out basis at reasonable cost.

Details of the proposed regulations are set out in the Attachment.

The proposed regulations would commence on 1 July 2013.

This Minute recommends that regulations be made in the form proposed.

Authority: Section [#] of title of Act

[Minister's initials]

**Details of the proposed *Superannuation Legislation Amendment Regulation 2012*
(No.)**

Proposed Schedule 1, item 1

Significant event notice – where replacement of MySuper is recommended by the trustee or an associate of the trustee

The proposed regulation prescribes that where the trustee or an associate of the trustee suggests or recommends to a member of a MySuper product that they transfer their interest in the MySuper product to any other product, whether it is another MySuper product or a choice product, the trustee or the associate of the trustee must provide a significant event notice to that member. The significant event notice must specify the changes to the member's interest that will result from transferring to another product regardless of whether the information was contained in the product disclosure statement (PDS).

Section 1017B of the Corporations Act provides that a notice must be given 30 days prior to a change in fees or charges. This is consistent with requirement in the Superannuation Legislation Amendment (MySuper Core Provisions) Bill 2012 which requires consent in writing to a transfer from a MySuper product no more than 30 days before a transfer occurs. This ensures the member, prior to deciding to provide consent, is informed of the changes to their interest that will result from transferring to another MySuper product or to a choice product.

Proposed Schedule 2, items 1 and 2

Requirements for benefits in respect of death

Section 32C of the SGA Act sets out the circumstances in which employer superannuation contributions satisfy the choice of fund requirements of the SGA Act.

From 1 July 2013, paragraph 32C(2)(d) of the SGA Act will state that, in order for superannuation contributions to satisfy the choice of fund requirements, the relevant fund must comply with requirements in the SGA Regulations in relation to insurance in respect of death. Specifically, in respect of fund members who are not MySuper members, the SGA Act will state that funds must comply with requirements in the SGA Regulations in relation to the offering of death benefits. In respect of MySuper members, funds will have to comply with requirements in the SGA Regulations in relation to the provision (rather than offering) of death benefits. This will reflect the requirement, which will be contained in section 68AA of the SIS Act, that trustees must ensure their funds provide benefits for death in respect of MySuper members by taking out insurance.

Regulation 9A of the SGA Regulations sets out the minimum levels of life insurance funds are currently required to offer their members in order to comply with the choice of fund requirements. It is proposed to amend regulation 9A to reflect the requirements that will be contained in paragraph 32C(2)(d) of the SGA Act. This

would involve a reference to actually providing death benefits in respect of MySuper members, rather than merely offering death benefits (which would apply in respect of other members).

It is also proposed to amend regulation 9A to reflect the requirement, which will be contained in section 68AA of the SIS Act, to allow MySuper members to elect that death benefits not be provided in respect of the member by the fund. While the regulation would now require funds to provide a minimum level of death benefits in respect of MySuper members, in order to comply with the choice of fund requirements, there would be an exception for cases where a member has elected that the benefits will not be provided or, if it is permitted by the fund, the member electing to hold a lower amount of life insurance.

The proposed amendments would take effect on 1 July 2013.

Proposed Schedule 3, items 1 and 3

Meaning of permanent incapacity

It is proposed that the existing definition of permanent incapacity in the SIS Regulations would apply for the purposes of the SIS Act.

The Superannuation Legislation Amendment (Further MySuper and Transparency Measures) Bill 2012 amended subsection 10(1) of the SIS Act to insert a definition of permanent incapacity. This definition will be used in defining the types of insured benefits trustees must provide MySuper members of regulated superannuation funds.

The subsection 10(1) definition of permanent incapacity will state that “a member of a regulated superannuation fund is suffering permanent incapacity if the member is taken, under the regulations, to be suffering permanent incapacity for the purposes of this Act”.

Currently, subregulation 6.01(2) of the SIS Regulations contains a definition of permanent incapacity, which applies to Part 6 and Schedule 1 of the SIS Regulations, dealing with payment standards and conditions of release of benefits, respectively. It is proposed to move this definition to a new regulation 1.03C to allow it to be employed for the purpose of subsection 10(1) of the SIS Act in addition to its existing applications.

The proposed amendment to the SIS Regulations would take effect on 1 July 2013.

Proposed Schedule 3, item 2, regulation 4.07D

Operating standard – self-insurance

From 1 July 2013, paragraph 31(2)(eb) of the SIS Act will allow operating standards to be prescribed in relation to the kinds of benefits that must not be provided other than by taking out insurance, or insurance of a particular kind.

It is proposed to prescribe an operating standard under which trustees of regulated funds would not be permitted to provide insured benefits that satisfy the conditions of

release for death, terminal medical condition, permanent incapacity or temporary incapacity in the SIS Regulations unless they are backed by an insurance policy. Under the proposed operating standard on types of insured benefits, these are the only types of insured benefits that will be able to be provided where the trustee of a superannuation fund enters into an insurance contract for the provision of benefits to beneficiaries of the fund.

The proposed prohibition on self-insurance would not apply to the provision of insured benefits to defined benefit members of funds (or sub-funds) that, as at 1 July 2013, are self-insuring in respect of their defined benefit members and are not prohibited from doing so by means of a condition on their trustee's licence.

The proposed prohibition would also not apply to the trustees of any fund where the insured benefits are provided by or their provision is guaranteed by the Commonwealth Government or the government of a State or Territory.

In addition, where a beneficiary is receiving benefit payments, has made a claim for benefit payments, or has experienced an insured event, during the period when self-insurance is permitted in respect of their fund, that beneficiary's ability to continue to receive benefit payments, to lodge a claim, to have a claim determined or to have further benefits paid would not be affected.

The proposed operating standard would reflect concerns raised in the Super System Review, which concluded there are significant risks associated with self-insurance as it is not subject to the same prudential requirements as those that apply to life insurance companies.

Where the governing rules of a fund do not permit a trustee to obtain an external insurance policy in respect of benefits previously self-insured the proposed standard would, if necessary, deem the governing rules to be amended to allow the trustee to obtain such a policy.

The proposed operating standard would take effect from 1 July 2013. Where the proposed standard would act to prohibit self-insurance in respect of a fund or sub-fund that is self-insuring as at that date, the trustee would have until 1 July 2016 to cease self-insuring.

Proposed Schedule 3, item 2, regulations 4.07C and 4.07E

Operating standard – permitted types of insurance

From 1 July 2013, paragraph 31(2)(ea) of the SIS Act will allow operating standards to be prescribed in relation to the kinds of benefits that must not be provided by taking out insurance, or insurance of a particular kind.

It is proposed to prescribe an operating standard under which, where the trustee of a regulated superannuation fund enters into an insurance contract for the provision of insured benefits to beneficiaries of the fund, the fund is prohibited from providing members with insured benefits other than those that satisfy the conditions of release at Schedule 1 of the SIS Regulations for death, terminal medical condition, permanent incapacity and temporary incapacity.

The proposed prohibition would apply in respect of regulated superannuation funds.

The proposed prohibition would not apply to the continued provision of insured benefits to members who joined a fund before 1 July 2013 but were not covered in respect of that insured benefit before 1 July 2013. This exemption only extends to circumstances where a member was covered in respect of an insured benefit prior to 1 July 2013, even where an insured event had not occurred. Therefore, the existing insurance arrangements in respect of beneficiaries who had joined the fund prior to 1 July 2013 would not be affected.

The proposed restrictions on providing types of insured benefits would only apply in respect of benefits that are provided by taking out an insurance contract with an external party.

In addition, where an approval has been granted, prior to 1 July 2013, under subparagraph 62(1)(b)(v) of the SIS Act for the provision of and release to beneficiaries of particular insured benefits, those benefits would be exempted from the restrictions on providing types of insured benefits. This proposed exemption would include the provision of such benefits to beneficiaries who joined the fund from 1 July 2013. The exemption would only apply while the approval under subparagraph 62(1)(b)(v) remains in force.

Where a trustee is unable to amend the governing rules of a fund to comply with the proposed restrictions on providing insured benefits, it is proposed that those terms of the governing rules would be deemed to be omitted from the governing rules and replaced by terms that allow the provision of benefits that are permitted.

The purpose of the proposed operating standard is to ensure the insured benefits that are available through superannuation for new beneficiaries are consistent with retirement incomes policy.

Currently, superannuation funds offer a range of benefits to members as permitted by the core and ancillary purposes of the sole purpose test at section 62 of the SIS Act.

The wording of section 62 allows funds to offer insured benefits that are not consistent with retirement incomes policy (as reflected in the conditions of release in Schedule 1 of the SIS Regulations). As a result, they cannot be released to members at the time of their disability, when the insurer makes a payment to the fund under the relevant insurance policy.

The proposed operating standard would take effect from 1 July 2013.

Proposed Schedule 3, items 4 and 5

Successor fund transfer rules not to apply to the transfer of accrued default amounts

The proposed amendment provides that transfers required under prudential standards are permitted by regulation 6.29 of the SIS Regulations, which relate to the transfer of member benefits to another fund (for example, in a fund merger situation).

This is necessary as prudential standards are of no effect to the extent that they conflict with the regulations. Therefore, transfers under prudential standards would have to otherwise satisfy one of the existing requirements of regulation 6.29.

The successor fund transfer rules will not apply to the transfer of accrued default amounts to a MySuper product in another fund. A prudential standard, made under section 34C for the purpose of section 29SAA, 29SAB, 387, 388 or 394 of the SIS Act, will require the transfer of the accrued default amounts to another fund in the following circumstances:

- Paragraphs 29SAA(1)(b) and 387(1)(b) require the trustee to take the action required under the prudential standards in relation to accrued default amounts where the trustee has sought MySuper authorisation but the member is not eligible to be in the fund's MySuper product.
- Section 29SAB requires action to be taken under the prudential standards if the authorisation to offer a MySuper product is cancelled under subsection 29U(1).
- Section 388 requires the trustee to take the action required by the prudential standards if the trustee holds accrued default amounts and has not applied for MySuper authorisation before 1 July 2017.
- Section 394 requires trustees that are not authorised to operate an eligible rollover fund at 1 January 2014, to transfer the amounts held in existing eligible rollover funds to an authorised eligible rollover fund or a fund that offers a MySuper product in accordance with the prudential standards.

Proposed Schedule 1, item 2, and Proposed Schedule 3, item 6, regulation 9.46

Notification – accrued default amount attributed to MySuper product

The proposed amendment would require trustees to provide members with a notice 90 days prior to attributing an accrued default amount to a MySuper product in the fund, or transferring that accrued default amount to another fund because the member is not eligible to hold a MySuper product offered by that fund. The notice must be provided 90 days in advance of the attribution occurring to provide members with a reasonable period to opt-out if they wish, and to ensure the currency of information in the notice.

The notice must mention the following:

- the amount that will be attributed;
- the name of the MySuper product to which the amount will be attributed;
- how the member may obtain a PDS for the MySuper product; and
- any other information the RSE licensee considers the member needs to understand the attribution.

However, where the attribution of the accrued default amount would result in one or more of the following:

- an increase in a fee or charge that applies to the amount;
- a reduction in an insured benefit;
- an increase in an insurance premium attributable to the member; or
- a change in the investment strategy that relates to the amount.

The notice must instead mention the following:

- the amount that will be attributed;
- the name of the MySuper product to which the amount will be attributed;
- how the member can elect, in writing, to opt out of the attribution;
- how the member may obtain a PDS for the MySuper product;
- any change to fees or charges that applies to the amount;
- any change to the member's insured benefits as a result of the attribution;
- any change to the investment strategy applicable to the amount as a result of the attribution; and
- any other information the RSE licensee considers the member needs to understand the attribution.

Fees and charges must be expressed in dollars except where ASIC determines that due to the nature of the fee and the charge can be expressed in another way.

Schedule 1, item 1 amends the Corporations Regulations to ensure that where an RSE licensee is required to provide this notice they will not also have an obligation to provide a significant event notice that would usually be required by section 1017B of the Corporations Act.

Proposed Schedule 3, item 6, regulation 9.47

Opt-out insurance covering MySuper members cannot be obtained at reasonable cost

The proposed regulation provides that life and TPD insurance must be offered on a compulsory basis for MySuper members if the trustee is reasonably satisfied that the insurance cannot be provided on an opt-out basis at reasonable cost.

Subsection 68AA(7) of the Superannuation Legislation Amendment (Further MySuper and Transparency Measures) Bill 2012 provides that regulations may specify conditions where funds are not required to provide members holding a MySuper product with the ability to opt-out.

The proposed regulation relates to risks in respect of life and TPD insurance being offered on an opt-out basis.