6 May 2019

The Manager
Retirement Incomes
The Treasury
Langton Crescent
PARKES ACT 2600

Email: superannuation@treasury.gov.au

Dear Sir/Madam

Universal terms for insurance within MySuper

Thank you for the opportunity to provide feedback to this consultation paper.

ASFA, AIST and the FSC are the joint Code Owners of the Insurance in Superannuation Voluntary Code of Practice (**Code**). More than 95% of MySuper members are members of funds that have signed up to the Code.

We have been collectively committed to developing and improving industry standards since setting up the Insurance in Super Working Group in late 2016. We have been considering the scope and potential for industry standardisation of terms for some time.

We have been carrying out this work in several stages. The first stage was to standardise headings for TPD, to assist with consumer understanding of their coverage at a high level. This is contained in the Code. The headings used are based on similar work undertaken in the United Kingdom.

We have established a sub-committee of trustee and insurer representatives to assist with the development of further standardisation. We are in a position to lead this work alongside Treasury, with the input and imprimatur of the life insurance and superannuation industries.

We are pleased to enclose our views on the questions posed as part of this consultation. We look forward to working with you closely on this project.

Should you wish to discuss any matters contained in this submission, please contact our Secretariat in the first instance, Sarah Phillips, at sarah@phillipsadvisory.com.au or 0498 494 791.

Yours faithfully

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Chief Executive Officer	Deputy CEO	Director of Policy
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1. What are the costs and benefits of standardisation of terms and definitions for default MySuper group life policies?

To properly determine the costs and benefits, it is important to first clearly define what is being standardised. This could involve standardising labelling and descriptions of common terms, which the Code Owners support and which is the focus of this submission. Standardisation could also encapsulate having legislated fixed cover, which we not support, as the potential costs noted below are likely to outweigh any consumer benefits.

We believe that the objectives of universal terms, definitions and exclusions should be:

- To assist members to compare cover offered by different funds
- To provide default cover that balances appropriateness and affordability, and gives comfort to members that they have appropriate insurance without having to research or have a technical understanding of insurance terms
- To provide minimum standard cover, to reduce complexity and to provide greater certainty to members
- To increase community understanding of life insurance products and terminology, by creating a level of consistency that allows for knowledge to develop over time regardless of an individual's particular policy – similar to the way that many general insurance terms such as "excess" are readily understood
- To ensure the benefits of standardisation outweigh the impact on premiums
- To increase protections to consumers from misconduct or conduct that falls below community standards and expectations.

In order to meet these objectives, we believe the scope of what should be standardised is as follows:

- Terms that are in common usage, to ensure consistency both in labelling and in meaning
- Statement of purpose of Total and Permanent Disability (TPD), including consideration of changing the title to better reflect the purpose
- Elements that make up TPD and terminal illness cover – i.e. "unlikely", "unable" – so that trustees would be able to offer cover made up of various standardised elements
- Removal of opinion clauses to create objective assessments and shift the balance of power away from insurers
- Evidence taken into account in assessment, up to when the claim is assessed.

Depending on the scope of standardisation, the potential costs are as follows:

- Premium impacts, where standard terms are more generous than a fund currently uses
- Competition impacts, where trustees cannot compete on generosity of cover
- Constraints on trustee discretion, if standard terms limit a trustee's ability to offer the cover it wants
- Mispricing, where a change of definition has no historical claims experience
- Reduction of member benefits, if standard terms result in a trustee offering less generous cover
- Consumer confusion, if standard definitions are not in alignment with legislative or regulatory definitions
- Legal interpretation risk, if courts or AFCA interpret a definition different to the industry's intention
- Cost of negotiating and implementing standard terms both at a fund and industry level.

2. What terms and definitions would benefit from standardisation? Are there particular terms/definitions where the case for standardisation is stronger or should be prioritised?

We suggest working with Treasury, regulators, external dispute resolution bodies and consumer advocates to determine the terms that cause consumer confusion, and undertake an audit of funds' existing terms in use. This work should determine prioritisation.

The objectives of this process would be to identify:

(1) where funds use different labels to mean the same thing, and
(2) where funds use the same label but with different meanings.

Using this process to achieve standardisation is supported, subject to appropriate management of the cost impact by the stakeholders involved in this process. The process needs to strike the balance between appropriate standardisation and the need for some flexibility for funds.

Any standardisation of wording should be consumer tested before it is finalised. We are open to the development of new labels to describe terms, if these are easier for consumers to understand.

Examples of terms that could be standardised:

- Income Protection/Salary Continuance
- Active Employment/At Work
- Limited Cover/New Events Cover
- Exclusions (such as Pre-Existing Condition exclusions)
- Salary/Income/Pre-disability Income
- Offsets
- Illness/sickness
- Injury
- Waiting period/Extended period
- Member/Insured
- Benefit/Payment
- Medical practitioner
- Working days/working hours
- Reasonable re-training
- Occupation and usual occupation
- Employed/working

For Income Protection, consideration should be given to the standardisation of certain key terms and definitions including the use of "own occupation" and "usual occupation" to provide clarity to members lodging an IP claim.

3. Should trustees be permitted to offer TPD insurances that differs from the definition of 'permanent incapacity' in the SIS Act? Is the current legislated definition of 'permanent incapacity' an appropriate standard definition of TPD?

Trustees should be able to offer different TPD cover to the SIS Act definition of "permanent incapacity", as they serve different functions. The SIS Act definition is used to determine whether a member can receive an early release of their superannuation account balance. This needs to be appropriate for all members, including those who may not have insurance. It would be an unfortunate member outcome if the requirement for account balance release was tightened as a result of the standardisation work. Trustees' TPD definitions should not prevent the release of a benefit from an account, where a member has met the SIS Act terms of release.

TPD definitions are tailored by trustees and insurers, taking into account the specific needs and risk profile of the membership pool while remaining adaptable to case law and regulatory changes.

If "permanent incapacity" in the SIS Act was used in policies, it may result in broader cover and consequently higher premiums. This is because "permanent incapacity" in the SIS Act is broader than conventional TPD definitions. Broader cover may be detrimental to certain member pools, where it will result in excessive premium costs and erosion of superannuation account balances. Currently, trustees are able to determine the balance between the level of TPD insurance cover and the impact of premium costs on member accounts that is in the best interest of their members.

Once the industry standardisation work is complete, the SIS Act definition of "permanent incapacity" may need to be reviewed to determine whether better terms could be used, including whether "permanent incapacity/TPD" is the best terminology.

Standard definitions need to be regularly reviewed to ensure they remain up-to-date and fit-for-purpose, and this process is much more difficult to achieve if the definitions are enshrined in law. This is an important reason for the standard definitions to be owned by the industry rather than by government or regulators.

4. Should the definition of TPD allow for rehabilitation or return to work initiatives? Why/Why not?

We support rehabilitation, return to work and retraining initiatives being included in the minimum standard TPD requirements but balanced by a recognition of members' existing access to benefits. A potential description of the purpose of TPD is suggested below:

> *Designed to provide financial support when someone can permanently no longer work because of sickness or injury, in a job for which they are educated, trained or experienced, taking into account any rehabilitation and retraining that the member could undertake in the near future that the trustee considers appropriate.*

TPD definitions which incorporate reasonable rehabilitation requirements can improve claims experience and the sustainability of group TPD insurance.

Furthermore, under the Code, trustees can only offer insurance that falls within the 1% cap, which means many are unable to offer income protection as a default benefit. Income protection allows insurers to offer occupational rehabilitation to assist claimants to return to work. We would support this being offered as part of TPD cover where trustees have determined it is affordable and appropriate for their membership.

5. Is there a need for universal insurance exclusions in MySuper products? Why/Why not? If yes, should exclusions be standardised across all types of insurance provided within MySuper products? What standardised exclusions would deliver the greatest benefit to consumers?

We support this on the same principles provided under question 1. We suggest the work begins with standard labelling of exclusions, and then standard meanings could be considered. It is important to note that in group insurance, there are very few exclusions which apply to default cover.

Further to the above, we are of the view that exclusions which affect the sustainability of the relevant group insurance arrangement (e.g. death benefit exclusions in the event of a pandemic illness) and those which prevent self-destructive behaviour can be standardised.

6. What lead time would be required for the industry to implement standardised terms, definitions and exclusions if this reform was implemented?

Any changes to terms, definitions and exclusions would need to be built into a trustee's arrangement with its insurer. Rather than imposing one firm deadline for implementation, we suggest it would be more appropriate to require trustees to build the changes into their next insurance renewal cycle. This would reduce the possibility of a sharp premium increase across funds and reduce additional administrative costs that could be passed on to members.

In addition, it should be noted that the development of standardisation will take time, to account for consultation with stakeholders, consumer testing the proposed definitions, and production and delivery of educational materials. In the case of a similar initiative in the UK (which involved the standardisation of a TPD definition in relation to critical illness), it took approximately two years from proposal until completion by the Association of British Insurers. This may be indicative of the time it will take to complete a similar initiative here in Australia, subject to the actual scope of definitions, terms and exclusions that will be standardised.

7. To what extent would standardising terms, definitions and exclusions across MySuper products impact the price of premiums?

When amendments are made to product terms and these amendments are more generous than the terms that are currently offered, it usually results in an increase in the number of claims payable. When the number of claims payable increases this obviously raises claims costs which leads to an increase in premiums.

If any standardised terms, definitions or exclusions are:

- more lenient – premiums are likely to increase
- more complicated to assess (even if the wording is more generous for example an 'unlikely' TPD definition) – premiums may increase due to more resources or information which may be required to carry out the assessment
- set as a minimum standard – premiums are unlikely to change where a product already offers more generous terms.

8. Would the impact on premiums outweigh the benefits of standardising the definition of TPD, or other definitions, terms and exclusions?

Without knowing where standardised terms may land, it is difficult to know whether increased premiums would outweigh any benefits of standardisation. The convenience and simplicity that could be achieved through standardisation should be balanced with its impact on the affordability and sustainability of group insurance arrangements.

The industry has already taken a view that an affordable level of premiums is 1% of lifetime salary, as outlined in the Code.

We would caution that any standardisation of terms should consider whether it could lead to pricing impacts which would mean the 1% cap is exceeded, which overall may not be in members' best interests.

9. How could the impact on the price of premiums be mitigated, without incentivising the creation of 'junk insurance policies'?

Trustees design products that are appropriate for their membership or cohorts of membership and in a way that is easily understood by fund members. Trustees may have formed the view that it is in a member's best interest to have some insurance cover rather than none at all, which may mean applying a different definition for members who are not working or are working less than the majority of the membership. This approach can keep insurance costs sustainable for members.

If standardised definitions would lead to an increase in premiums, then the amount of cover offered may need to reduce. There is a delicate balance between amount of cover and cost of premiums, which needs to operate within the 1% cap.

10. If terms, definitions and exclusions for MySuper products were standardised, how long would repricing of premiums take to flow through to members?

It would be sensible to have a transition period to allow proper consideration of price impacts and to align with renewal periods (provided this process does not exceed three years) to avoid members experiencing a sharp increase in premiums later down the track. Otherwise, price implications of standardised terms and definition will necessarily immediately flow through to members.

For terms and definitions with limited claims experience to base premiums on, subsequent claims experience will also have to be factored in at a later time.

11. To what extent would standardised terms, definitions and exclusions for MySuper products improve consumer understanding of insurance in superannuation? What particular changes would deliver the greatest benefits to consumer outcomes?

We believe that consumer-tested, standard labelling would improve consumer understanding, by allowing for comparison between different funds' offerings, as well as managing expectations at claim time.

By standardising the components that make up cover, this will make default insurance as consumer friendly as possible while minimising the risks we have set out in our answer to question 1.

Legislated fixed cover may assist with understanding but could lead to poorer member outcomes due to the potential premium increase and other risks noted above.

Notwithstanding this, and as noted by all inquiries into financial services, most consumers have low levels of financial literacy, and insurance is no exception to this. While standardisation may improve consumer understanding, the extent of improvement will be limited. This is an important reason why the objective of standardisation must also include increasing protections to consumers from misconduct or conduct that falls below community standards and expectations.

12. Are there other ways to improve consumer understanding of insurance in superannuation without standardising terms/definitions/exclusions?

In the Code, one of the objectives is that communications to members will be clear, timely and in plain language, to assist understanding of the role of insurance in superannuation and the details of members' insurance cover.

As part of the process of implementing the Code, all funds and insurers are looking at ways to better engage members in order to assist with understanding. This has included developing a standard Key Facts Sheet for a fund's default offering, as well as consumer testing of a fund's key insurance concepts.

13. Should maximum, minimum or set levels of cover be prescribed for MySuper products? Why/Why not? Should these apply to all types of insurance provided within MySuper products?

It is our view that trustees are best placed to determine the appropriate levels of cover for their membership generally or cohorts therein, in accordance with their best interests duty, S. 52 (7) of the SIS Act and the requirements of the Code. This is a more appropriate response and better consumer outcome than legislating levels of cover.

The Code provides trustees with the necessary flexibility to make determinations about appropriate and affordable levels of cover based on their knowledge of their membership, within the bounds of a premium level that is no higher than 1% of salary.

If limits were to be prescribed this would limit trustees' ability to determine an appropriate level of cover to fulfil their best interest duty to members. It may also prejudice those members who are employed in high-risk occupations, given that those members may have to be underwritten to increase their cover is set levels of cover are low.

14. What factors should be taken into account if a minimum, maximum or set level of cover were to be prescribed?

Age is taken into account by funds in setting levels of cover and this should be the key factor in setting minimum levels of cover generally.

The cost of insurance cover has an impact on members retirement savings, and this should be a key factor in setting maximum levels of cover. As part of determining affordability the Code requires that in the design of insurance benefits for Automatic Insurance Members, premiums for this benefit design will be set at a level that does not exceed 1% of an estimated level of salary for fund membership generally, and/or for segments within the membership.

15. Are there any unintended consequences of mandating a minimum, maximum or set level of cover for MySuper products?

Yes, if the level of cover is mandated then the provision of insurance cover may be subject to adverse events in the insurance market and may result in insurers withdrawing from the market or cover becoming more expensive.

It will limit the trustees' ability to exercise their judgment in fulfilling their best interest duty to members. It may also result in over-insurance and under-insurance for some members. Members in different cohorts such as those employed in high-risk occupations may not receive cover appropriate to their circumstances.