

4 June 2018

By email: superannuation@treasury.gov.au

Manager, Regulatory Framework Unit
Retirement Income Policy Division
The Treasury
Langton Crescent
Parkes ACT 2600

Dear Sir/Madam,

Submission: Protecting Your Super package: Exposure Draft

Thank you for the opportunity to comment on the Exposure Draft of the *Treasury Laws Amendment (Protecting Superannuation) Bill 2018* (the **Exposure Draft**).

This submission focuses on insurance in superannuation. We have had the opportunity to review the submission made to this consultation by CHOICE and agree with CHOICE's following Recommendations.

- Recommendations 1 and 2 in relation to fees,
- Recommendations 3-5 and 8-10 in relation to insurance, and
- Recommendations 11 and 12 in relation to consolidating inactive accounts.

We have focused this submission on the interests of people who are on low incomes or have low superannuation balances. While many people experience account erosion because of superannuation fees and charges, the Productivity Commission's *Superannuation: Assessing Efficiency and Competitiveness (Draft Report)*, dated April 2018 (**Draft Report**), states that balance erosion due to insurance premiums 'can be excessive and highly regressive—having a disproportionate impact on members with low income, intermittent labour force attachment and/or multiple accounts with insurance'.¹

However, insurance cover can also provide significant financial protection to vulnerable people. Given this, while we support much of the reform package proposed by the Exposure Draft, we consider that a sophisticated approach is needed to understand the demographics of superannuation members and their insurance requirements.

We note that the Productivity Commission's Draft Report is of significant relevance to these reforms. We have not provided detailed analysis of the Draft Report, due to the timing of its release.



¹Productivity Commission, *Superannuation: Assessing Efficiency and Competitiveness*, April 2018, p 311, available at: <http://www.pc.gov.au/inquiries/current/superannuation/assessment/draft>.

About Consumer Action Law Centre and Financial Rights Legal Centre

Consumer Action Law Centre is an independent, not-for-profit consumer organisation with deep expertise in consumer laws, policy and direct knowledge of people's experience of modern markets. We work for a just marketplace, where people have power and business plays fair. We make life easier for people experiencing vulnerability and disadvantage in Australia, through financial counselling, legal advice, legal representation, policy work and campaigns. Based in Melbourne, our direct services assist Victorians and our advocacy supports a just market place for all Australians.

The Financial Rights Legal Centre is a community legal centre that specialises in helping consumers understand and enforce their financial rights, especially low income and otherwise marginalised or vulnerable consumers. We provide free and independent financial counselling, legal advice and representation to individuals about a broad range of financial issues. Financial Rights operates the National Debt Helpline, which helps NSW consumers experiencing financial difficulties. We also operate the Insurance Law Service which provides advice nationally to consumers about insurance claims and debts to insurance companies

Recommendations

We agree with the following recommendations in CHOICE's submission to this consultation:

- Recommendations 1 and 2 in relation to fees,
- Recommendations 3-5 and 8-10 in relation to insurance, and
- Recommendations 11 and 12 in relation to consolidating inactive accounts.

In addition, we recommend that:

- The exemption of buy-sell spread fees from the ban on exit fees be removed.
- Alternatively, if buy-sell spread fees continue, they must be:
 - cost-reflective across all types of superannuation funds,
 - clear, transparent and available to all fund members, and
 - identified in the Product Disclosure Statement and other documents and communications as a cost of exiting the fund.
- The removal of default insurance for accounts with balances below \$6,000 only apply to inactive accounts.

Schedule 1: Fees charged to superannuation members

Cap on fees

We welcome moves to prevent the erosion of superannuation account balances through high fees under Schedule 1 item 16 of the Exposure Draft. This is a critical risk for people who have low incomes and low superannuation account balances. The effectiveness of the fees cap will be significant in protecting the retirement incomes of the people who we work with.

We support CHOICE's position as follows:

- A cap on fees for superannuation accounts with a balance of less than \$6,000 is necessary. However, we share CHOICE's concerns about how the 1.5 percent cap per six-month period was determined, and whether this is fair and appropriately protecting people's account balances.



- A twice-yearly balance test is necessary to prevent people's superannuation quickly eroding.
- If people are charged excess fees, these must be rebated. The rebates must include the equivalent investment earnings on the amount rebated.
- The legislation should be framed broadly to prevent 'gaming' of the cap and unintended circumvention of the cap.
- The regulator should monitor superannuation funds' implementation of the fee cap to ensure compliance and report on its operation. With average fees sitting at just one percent, regulatory efforts should be strong and focused on preventing avoidance of the law and/or a 'race' to the cap.

While regulations may prescribe a fee cap of lower than 1.5 percent per six-month period under proposed section 99G(3), there should be a formal mechanism for regular review to ensure that the cap is working and appropriate.

Exit fees

We largely support the ban on exit fees under Schedule 1 item 13 of the Exposure Draft. We echo CHOICE's comments on exit fees, in particular:

- exit fees should be banned as they are a barrier to consumer-side competition;
- buy-sell spread fees are opaque and difficult to determine; and
- the implementation of the exit fee ban should be monitored by the regulator.

Superannuation is by nature a complex product with low consumer engagement. The Productivity Commission's in its Draft Report found that most people are not engaged with their superannuation, and are not always going to make the best decisions about it. The Draft Report stated:

... low engagement is to be expected in a compulsory and complex system that covers the bulk of the population... But in many respects the system—and government—has made engagement harder than it ought to be for members.²

People who rollover their superannuation account balances should not be presumed to be 'engaged' consumers who are making a well-informed decision about their superannuation. People may rollover their accounts simply because they were given a prompt at the end of their online income tax return process. We should not assume that people who shift their account balances understand the fees charged when they move their balance, and the impact this will have on their retirement incomes. Therefore, if funds continue to charge buy-sell spread fees, regulation should take a predominantly 'product safety' approach, rather than one based on transparency and disclosure to the consumer.

We also question the rationale for excluding buy-sell spread fees from the definition of exit fees under proposed section 99BA(2). These are difficult to attribute to a particular member and therefore should generally be considered a part of the administration of the fund and fall within the definition of administration fees. Such separate transactional fees clearly operate as a barrier or drawback to people consolidating their superannuation accounts.

² Productivity Commission *Draft Report: Overview—Superannuation: Assessing Efficiency and Competitiveness*, April 2018, p 23.



At a minimum funds should only be able to charge buy-sell spread fees upon exit that reflect the fund's actual costs of the transactions, as is currently the case for MySuper Products under section 99C of the *Superannuation Industry (Supervision) Act 1993*. In other words, the existing requirement applying to MySuper funds should apply to all funds.

If these fees are to remain separately identified they should also be identified as what they are—the cost of exiting the fund.

Recommendations

- That the exemption of buy-sell spread fees from the ban on exit fees be removed.
- That, alternatively, if buy-sell spread fees continue, they must be:
 - cost-reflective across all types of superannuation funds; and
 - clear, transparent and available to all fund members; and
 - identified in the Product Disclosure Statement and other documents and communications as a cost of exiting the fund.

Schedule 2: Insurance for superannuation members

Our key consideration in assessing these reforms is ensuring that people who are financially vulnerable continue to be assisted by insurance in their superannuation, while not being adversely affected by superannuation account erosion due to high insurance premiums.

We note that APRA and the Australian Securities & Investments Commission (**ASIC**) have released figures with respect to life insurance claims data and, in particular, life insurance available via group insurance. These figures show 15,165,000 lives were insured under group insurance. The collection found that for the period of 1 January 2017 to 30 June 2017 there were 9,565 death benefit claims, 16,377 total permanent disability claims and 16,112 disability income insurance claims in group insure—miniscule numbers when considering the numbers covered, and the premiums paid (\$6.8 billion).³ These figures suggest that there is significant scope for cover to be offered at more affordable rates.

We support CHOICE's views that:

- There is a fundamental need for protections for people who are unable to provide financially for their families due to illness, disability or death. Private life insurance in superannuation is a limited form of protection.
- Bundling life insurance products in superannuation is a barrier for people to make decisions about insurance and this advantages insurers. We would also add that bundling forces people to pay for unsuitable insurance—for example, a young person without dependents who is working in a high-risk job may need income protection and disability/trauma insurance, but is unlikely to need death cover.
- A balance needs to be struck between financial protection of people in the case of disability, illness or death, and erosion of account balances.

³ APRA, *Response to Submissions, Life insurance – public reporting of claims information – update on progress*, 24 May 2018.



We also support CHOICE's recommendation that the Government conduct a broader review of these reforms alongside alternative models to protect people who are unable to work due to disability.

We reiterate the Productivity Commission's view that superannuation is by nature a product that people are not engaged with strongly.⁴ This means an effective 'product safety' and suitability approach is critical in the regulation of insurance in superannuation.

No default insurance for people under 25 years

On balance, we support this reform proposed by new section 68AAC.

We support CHOICE's views that that:

- protections are needed to prevent discrimination against members in this demographic who wish to take out insurance, including a community rating system, and
- these reforms should be reviewed in four years to assess how effectively they balance the needs and costs for young people.

Workers compensation schemes may cover many younger people in high risk work. However, if the Government's view is that private life insurance is an important financial protection, this insurance must be accessible and affordable for the young people who need for it. This will include young people with dependents and/or in high risk work.

No default insurance for accounts with balances below \$6,000

While we acknowledge the significant impact of balance erosion on low-balance accounts, we only support the move away from default insurance on accounts with balances under \$6,000 for accounts which are *inactive*. We therefore do not support proposed section 68AAB under Schedule 2 item 1 of the Exposure Draft in its current form.

There are many reasons that a person may have a balance below \$6,000. It may be because they have multiple accounts, recently returned after an extended period away from work, recently arrived in Australia, or their employer has not paid employer contributions. These could all occur with active accounts. While insurance premiums will significantly erode low balances, it does not follow that people with low balances do not need insurance.

It may be suggested that the disability support pension replace a significant proportion of income for people on low incomes should they be unable to work due to a disability. However, a person's income level is not the only consideration in whether insurance is suitable for them. For example, a person working part-time and also providing unpaid care to a family member is making a significant non-financial contribution to their family. If that person was unable to work and provide unpaid care due to disability or death, the impact on their family of their unpaid care no longer being given may be more significant than their lost income.

⁴ Productivity Commission *Draft Report: Overview--Superannuation: Assessing Efficiency and Competitiveness*, April 2018, p 23.



We note that the Productivity Commission’s Draft Report recommended that people have one superannuation fund which moves with them between jobs.⁵ Until this recommendation and the rollover of inactive accounts proposed under this Bill (see below) are implemented, the distinction between inactive and active accounts is significant, particularly for vulnerable people on low incomes.

Recommendation

That the removal of default insurance for accounts with balances below \$6,000 only apply to inactive accounts.

Cancellation of insurance on inactive accounts

In relation to insurance on inactive accounts, we note again the Productivity Commission’s finding that balance erosion is highly regressive in its impact—that is, it is more costly to members with low incomes.

We support the general rationale for cancelling insurance on accounts which have been inactive for 13 months. In an environment where large numbers of small accounts are being eroded by insurance premiums, negatively impacting upon the retirement savings of Australians, action to stem this flow is long overdue.

We do however wish to note the impact of the proposed section 68AAA under Schedule 2 of the Exposure Draft upon the most vulnerable of people in the community.

For example, someone who unexpectedly takes time out of work to care for an ill relative may need death and disability cover, even if they would be ineligible to claim on income protection cover. There are other people whose disability, injury or circumstance will necessarily lead to disengagement (intended or otherwise) with their superannuation and insurance, and consequentially inactivity in their account. These people—who may need this insurance the most—may have this removed.

Financial Rights regularly hears from consumers who are eager to maintain their super accounts for the purposes of life insurance cover. The following case study, while also involving the loss of benefits arising out of the age cut-off, is indicative of the attitude that exists towards inactive super accounts.

Madelaine’s story (Financial Rights case study)

Madelaine wrote to the Insurance Law Service distressed that she was about to lose access to her life insurance held via her superannuation. She said that she had life insurance in superannuation for the past 30 years and was about to lose it because she was turning 65. Her Super account balance was only \$1,400. Her account had been inactive from caring for her war veteran husband for many years. She had kept it though because she explicitly wanted to hold on to her life insurance—indeed it was the only way she could afford life insurance.

⁶ Legal Aid News, 1 June 2018, <https://news.legalaid.nsw.gov.au/pub/pubType/EO/pubID/zzzz5b0f69e70aa76040/?aid=87c7b763109c84c1Wc7b763109c84c1>.



Legal Aid NSW also reports that they assisted a man experiencing homelessness to successfully claim on his Total and Permanent Disability (TPD) insurance in his superannuation.

Legal Aid NSW case study

Legal Aid NSW has secured a \$140,000 payout for a homeless man who did not realise he had superannuation insurance. The man, whose job involved physical labour, received worker's compensation for a time after his previous lawyer successfully argued that his condition was aggravated by his work. After flooding in the northern NSW town where the man lived left him homeless, he visited a homeless legal advice clinic, seeking help to manage his debts.

Legal Aid NSW provided advice in relation to the debts and also asked questions about the man's work history. Further enquiries at the Australian Taxation Office (ATO) revealed the man had a superannuation fund, and Legal Aid NSW was able to submit a TPD claim. The \$140,000 claim was recently approved—a great result for the client and a reminder to lawyers to ask about their clients' work history.⁶

A better understanding of member demographics and the reasons for an account being inactive would minimise the risks of people who stand to benefit from the insurance inadvertently losing cover.

That said, and as discussed further below, we recognise that is expected that regulations will require trustees to provide written notification from 1 July 2019 to members whose accounts have been inactive for six or nine months. This is designed to communicate that if the account continues to be inactive for a total of 13 continuous months, insurance will be only offered or maintained on an opt in basis. If such communications were effective, they may operate to ensure someone in the position of Madeline doesn't lose access to insurance.

Communication about changes to insurance

We support CHOICE's view that communications by trustees to consumers regarding changes to insurance cover, as anticipated under the regulations,⁷ must be consumer tested.

We note again the 'disengaged' nature of superannuation consumers, which is notable in the context of communications conveying complex information. A behavioural economics approach is necessary in drafting and sending these communications, and 'nudge' techniques must be used to maximise the chance of people acting appropriately on the communications.

We also note the product safety approach is relevant here. That approach would see default insurance coverage based on a more sophisticated understanding of demographics. This is preferable to coverage based on disclosure and active opting-in, which places the onus on the consumer to assess their own insurance needs.

⁶ Legal Aid News, 1 June 2018,

<https://news.legalaid.nsw.gov.au/pub/pubType/EO/pubID/zzz5b0f69e70aa76040/?aid=87c7b763109c84c1Wc7b763109c84c1>.

⁷ Explanatory Memorandum to the Exposure Draft, paras 3.19-3.20.



The appropriate forms of consent will soon be developed in relation to the Consumer Data Right. This work will have broader relevance to communications which require people to consider their own interests and respond appropriately.

'Inappropriate erosion' of balances

We support the recommendation of CHOICE that there be clearer obligations on trustees to avoid 'inappropriate erosion' of balances by insurance premiums. This should be based on a more detailed understanding of the demographics and insurance needs of members, not simply their age and/or account balance.

Schedule 3: Consolidation of low-balance inactive accounts

We broadly support the amendments under Schedule 3 of the Exposure Draft to consolidate inactive low balance accounts into active accounts.

We agree with CHOICE that:

- the consolidation of low-balance inactive accounts will have a significant impact on the retirement savings of Australians,
- the Australian Taxation Office (**ATO**) should be appropriately funded to undertake this work and that mandated timelines be put in place, to ensure taxpayer trust, and
- that disputes with the ATO regarding funds fall within the remit of the Australian Financial Complaints Authority, to ensure free and timely dispute resolution.

Please contact Susan Quinn on 03 9670 5088 or at susan@consumeraction.org.au or Drew MacRae on 02 8204 1386 or drew.macrae@financialrights.org.au if you have any questions about this submission.

Yours sincerely



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