

April 2019

# Submission in Response to Treasury Issues Paper on Universal Terms for Insurance within MySuper

## ABOUT US

The **Superannuation Consumers' Centre** was formed in 2013 as a not-for-profit to advance and protect the interests of superannuation consumers. The SCC aims to educate, advocate on behalf of and directly assist superannuation consumers to improve the standard of living for people of retirement age.

We work in partnership with CHOICE; the consumer advocate that provides Australians with information and advice, free from commercial bias. CHOICE fights to hold industry and government accountable and achieve real change on the issues that matter most.

To find out more about CHOICE's campaign work visit [www.choice.com.au/campaigns](http://www.choice.com.au/campaigns)

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, and the Mob Strong Debt Help services which assist Aboriginal and Torres Strait Islander Peoples with credit, debt and insurance matters. Financial Rights took close to 25,000 calls for advice or assistance during the 2017/2018 financial year.

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## Table of Contents

Introduction	2
Summary of Recommendations	3
Meeting Community Expectations	4
Benefits of Standardisation	6
Focus on Total and Permanent Disability (TPD) Terms, Definitions and Exclusions	9
Cost of Standardisation	13

## Introduction

At its core, insurance in superannuation should be about protecting people and their families when a person can no longer work due to death or disability. With the large variety of life insurance policy terms and restrictions, at best, people don't know what they are covered for and, at worst, they've been left with poor value, junk insurance.

Superannuation is a product that people regularly place as the most difficult purchasing decision to engage with,<sup>1</sup> yet it is one of the most important decisions they will make in their life. Given this importance, consumer protections need to be of a very high standard to prevent harm. Standardising key terms, definitions and exclusions will lead to clear and measurable gains to efficiency and equity. The benefits of standardisation outweigh any perceived costs of providing reasonable cover.

If you can no longer work due to disability, you shouldn't need a law degree to understand if your family will be protected. Yet, most policies require the additional overlay of legal precedent to understand what they mean. Members of the public who attempt an "apples to apples" comparison of insurance cover currently contend with the many subtle and opaque variations in terms, definitions and exclusions between different policies.<sup>2</sup> Independent academic research shows that simplifying product disclosure leads to better financial decisions.<sup>3</sup> Reducing the multitude of Total and Permanent Disability (TPD) definitions to a single understandable definition would be a big step in the right direction, especially given the context of chronically weak demand-side competition in the system.<sup>4</sup>

It's clear that the narrowness of many TPD definitions do not meet community expectations.<sup>5</sup> The community benefit of clear universal terms outweighs any perceived cost of standardisation. The current debate around universalising insurance cover is likely to raise fundamental questions about how best to provide for people in an affordable way and how life insurance interacts with other forms of protection, such as workplace insurance, the Disability Support Pension and the National Disability Insurance Scheme (NDIS). We see this as an important time to step back and assess how these different schemes interact and how best to protect people who can no longer work. To resolve these questions about insurance in superannuation there is a clear need to establish an independent inquiry into how best to deliver for people (and their families) who can no longer work due to death or disability.

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<sup>1</sup> CHOICE 2017, 'Consumer Pulse question – how complicated do you feel it is to find the product that best suits you?', 42% answered quite complicated or very complicated,

<sup>2</sup> ASIC, 2018, "Report 591: Insurance in Superannuation", p. 14

<sup>3</sup> Thorp et al, 2017, "Flicking the Switch: Simplifying Disclosures to Improve Retirement Plan Choices". Available at <https://ssrn.com/abstract=2783113>

<sup>4</sup> Productivity Commission, 2018, 'Superannuation: Assessing Efficiency and Competitiveness', p.57

<sup>5</sup> Ibid, p.408

## Summary of Recommendations

### **Recommendation 1**

That the Federal Government establish an independent inquiry into insurance in superannuation, with suggested terms of reference including:

- 1) An exploration of community expectations regarding the appropriate level and modes of financial support for people (and their families) who can no longer work due to death or disability.
- 2) Whether providing insurance through superannuation is the most efficient and equitable method for meeting community expectations for support of people (and their families) who can no longer work due to death or disability.
- 3) The degree to which more equitable standardised terms can co-exist with trustees' obligations not to "excessively erode" members' balances. This should include:
  - a. A robust assessment of the efficiency and equity benefits associated with standardised terms, definitions and exclusions that meet community expectations.
  - b. An assessment of the potential costs regarding implementing standardised terms, definitions and exclusions.
  - c. An assessment of the appropriate level and indexing of mandatory minimum levels of cover, based on community expectations of an acceptable minimum level of cover.
- 4) Whether the current regulatory regime is effectively ensuring members' best interests are met by the cover they are defaulted into.

### **Recommendation 2**

Standardise the definition of Total and Permanent Disability (TPD) to reflect the definition of permanent incapacity found in the SIS Act regulations.<sup>6</sup>

### **Recommendation 3**

Standardise the definition of the term "unlikely" in the SIS Act definition to mean "less than 50% chance" to ensure the interpretation of this term meets community expectations.

### **Recommendation 4**

Prohibit the use of the more stringent eligibility criteria (including but not limited to Activities of Daily Living and Everyday Work Activities tests) for TPD insurance.

### **Recommendation 5**

Prohibit policies which do not deliver TPD benefits as a lump sum as they have been shown to harm people who are receiving a benefit.

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<sup>6</sup> Superannuation Industry (Supervision) Regulations 1994 (Cth), regulation 1.03C

## Meeting Community Expectations

### We need to define why insurance in superannuation is provided

Few people engage with their superannuation,<sup>7</sup> fewer still engage with the default insurance product bundled within their superannuation.<sup>8</sup> In a properly functioning market, people would purchase a level of cover that met their needs at a price they could afford. In the default market, it is trustees that decide what level of cover is provided, with a constant pressure to ensure premiums are not unduly eroding people's retirement savings. Too often this has created a 'race to the bottom' as policies become more restrictive to stop erosion.

People need better protections in insurance in superannuation to ensure that the insurance they pay for is fit for purpose. The first step is to research, explore and define what the community expects this default insurance product to cover them for if they can no longer work or how it should support their dependents if they pass away. At the end of this process we may discover that the current system cannot provide the protection people deserve in an affordable, equitable way; this may lead to more fundamental questions about the best way to protect people who can no longer work or support their families.

The quality of cover for over ten million MySuper accounts with some form of insurance<sup>9</sup> varies substantially depending on the insurer. The current system has consistently failed to ensure cover meets community expectations. An inquiry into insurance cover was recommended by the Productivity Commission<sup>10</sup> and we see this as an important time to step back and establish an independent inquiry into how best to deliver for people who can no longer work due to disability.

While the funds and insurers now claim to be addressing the coverage problem through the Life Insurance in Superannuation Voluntary Code of Practice, the Productivity Commission inquiry found it "falls well short of what is considered best practice for an industry code of conduct", primarily as is not enforceable.<sup>11</sup> It was accurately assessed to have "all the bite of month-old lettuce"<sup>12</sup> by legal and consumer groups. The Code gives ultimate discretion to trustees in how or even *if* they choose to comply. The Code fails to help trustees understand community expectations in insurance design or appropriately manage the affordability and quality trade-offs.

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<sup>7</sup> Productivity Commission, 2018, 'Superannuation: Assessing Efficiency and Competitiveness', p.260

<sup>8</sup> Ibid, p.385

<sup>9</sup> APRA, 2018, "Annual MySuper Statistics, June 2018", Electronic Dataset. Available at <https://www.apra.gov.au/publications/annual-mysuper-statistics>

<sup>10</sup> Productivity Commission, 2018, 'Superannuation: Assessing Efficiency and Competitiveness', p.414

<sup>11</sup> Productivity Commission, 2018, 'Superannuation: Assessing Efficiency and Competitiveness', p.400

<sup>12</sup> Financial Review, 2016, "Life insurance claims data to be made public". Available at <https://www.afr.com/news/politics/life-insurance-claims-data-to-be-made-public-20161012-gs0gsj>

## Terms in insurance need to meet community expectations

Under the current system, we support the standardisation of key terms, definitions and exclusions.

Assuming insurance continues to be provided by default through MySuper products, it should meet community expectations of adequate and accessible cover. This is a far better approach than the current 'magic pudding' approach of hollowing out policies with fine print exclusions in order to keep premiums affordable. Recently released APRA claims data shows a 10 percentage point gap in the proportion of claims admitted for Total and Permanent Disability (TPD) cover between the two insurers with the greatest market share in the group super TPD policy market.<sup>13</sup> Further, there is a 22 percentage point gap between the insurer with the highest and lowest proportion of TPD claims admitted, respectively.

These wide gaps are indicative of a system which has allowed some policies to be hollowed out to the point that large numbers of people are being knocked back from cover, while others have been able to maintain relatively high successful claim rates. Keeping cover affordable by knocking back a large proportion of claims has a very serious risk of undermining the core purpose of insurance in superannuation. We need a better standard that delivers the help the community expects if people can no longer work.

Over time, but especially in response to poor financial performances by insurers in 2013, many TPD policies in MySuper products narrowed their definitions.<sup>14</sup> This was likely to mitigate the additional costs of a higher rate of TPD claims as more people discovered they had default insurance in superannuation.<sup>15</sup> Using a community expectations framework, it is clearly not acceptable to reduce the quality of cover simply because the insurer or fund has not properly designed its product to take account of real demand. People's needs remain fixed in the face of a disability, hollowing out policies to meet affordability concerns is a false economy, which will ultimately see people paying for cover that will never meet their needs when they need to make a claim.

### **Recommendation 1**

That the Federal Government establish an independent inquiry into insurance in superannuation, with suggested terms of reference including:

1. An exploration of community expectations regarding the appropriate level and modes of financial support for people (and their families) who can no longer work due to death or disability.

<sup>13</sup> APRA, 2019, "Life Insurance Claims and Disputes Statistics", Electronic Dataset. Available at <https://www.apra.gov.au/publications/life-insurance-claims-and-disputes-statistics>

<sup>14</sup> Australian Lawyers Alliance, 2018, "Submission in response to Policy questions arising from Module 6", p. 9-14. Available at <https://www.lawyersalliance.com.au/documents/item/1360>

<sup>15</sup> Sydney Morning Herald, 2016, 'Devils are in the detail in super life insurance'. Available at <https://www.smh.com.au/business/consumer-affairs/devils-are-in-the-detail-in-super-life-insurance-20160805-qqlnlk.html>

2. Whether providing insurance through superannuation is the most efficient and equitable method for meeting community expectations for support of people (and their families) who can no longer work due to death or disability.
3. The degree to which more equitable standardised terms can co-exist with trustees' obligations not to "excessively erode" members' balances. This should include:
  - a. A robust assessment of the efficiency and equity benefits associated with standardised terms that meet community expectations.
  - b. An assessment of the potential costs regarding implementing standardised terms.
  - c. An assessment of the appropriate level and indexing of mandatory minimum levels of cover, based on community expectations of an acceptable minimum level of cover.
4. Whether the current regulatory regime is effectively ensuring members best interests are met by the cover they are defaulted into.

## Benefits of Standardisation

### Consumers will benefit from standardisation

Currently, terms in group insurance can be so restrictive that they harm consumers. There is substantial variation in TPD definitions between funds.<sup>16</sup> Many definitions are substantially narrower than the definition of permanent incapacity in the Superannuation Industry (Supervision) Act ('SIS Act') Regulations.<sup>17</sup> Additionally, there is further variation between policies in terms of differing additional eligibility criteria and exclusions. The narrowness of these definitions, often coupled with restrictive eligibility criteria, means some people are being denied claims in situations where they will never be able to work again in a job for which they are "reasonably qualified by education, training or experience". Inconsistent definitions exacerbate the information asymmetry in insurance in superannuation. The insurer, their actuaries and lawyers understand the nuances of a slightly different definitions, however consumers do not.

Although there are still significant problems of conflicted remuneration in life insurance advice, people receiving individual-advised policies are in a much better position to select cover that matches their expectations and needs. They are also in a position to avoid the kinds of restrictive policy terms that have developed in group life insurance. This is borne out in the claims denial data, with a higher proportion of rejections for group superannuation policies due to not meeting contractual definitions (86.3%) relative to individual-advised policies (79.1%) according to recently released APRA claims data.<sup>18</sup> Again, this shows the need to better align life insurance in MySuper with community expectations.

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<sup>16</sup> ASIC, 2018, "Report 591: Insurance in Superannuation", p. 14

<sup>17</sup> Australian Lawyers Alliance, 2018, "Submission in response to Policy questions arising from Module 6", p. 9-14. Available at <https://www.lawyersalliance.com.au/documents/item/1360>

<sup>18</sup> APRA, 2019, "Life Insurance Claims and Disputes Statistics", Electronic Dataset. Available at <https://www.apra.gov.au/publications/life-insurance-claims-and-disputes-statistics>

### Case study – Darryl’s story

Financial Rights Legal Centre regularly receives queries about TPD definitions which can be confusing and difficult to discern. The following is a typical example we received via email on the Insurance Law Service:

*I am trying to make a TPD claim for a mental health condition. I understand my super fund re-defined TPD to include retraining and other occupation capabilities in 2014. Does this date apply to disability / illness / onset before that date? or apply to when the claim forms were first lodged which was after that date? At the last minute they brought this issue up. Your advice needed urgently as they are asking for assessment under new rule...*

*Source: Financial Rights Legal Centre*

There is a large efficiency cost to the proliferation of TPD definitions. People who attempt an “apples to apples” comparison of insurance cover must contend with the many subtle variations in terms between different policies. As ASIC report 591 found “a high level of variation in TPD definitions used in insurance products poses significant challenges for members in understanding and comparing insurance cover”.<sup>19</sup> Independent academic research shows simplifying product disclosure in retirement products leads to better financial decisions, particularly when people do not need to focus on relative risk and can focus on dollar costs.<sup>20</sup> Reducing the number of TPD definitions to a single, understandable definition, in addition to removing unnecessarily harsh eligibility criteria and terms, would be a big step in the right direction of simplifying the overall complexity of choosing the right insurance and ultimately MySuper product.<sup>21</sup>

There are major benefits to improving people’s ability to compare MySuper products. The Productivity Commission (PC) estimated the difference between a person in a bottom quartile and a top quartile performing fund could be \$502,000 by the time they retire.<sup>22</sup> At the moment, a person looking for a better performing fund or to consolidate existing funds may be dissuaded from making a decision because they are unsure of the impact on their insurance. Standardising cover will give people a much higher level of comfort about switching. Standardisation would allow product disclosures to focus on explaining the nature and extent of cover. Comparison would be limited to premiums and benefits, which are easier for people to assess. This issue should be

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<sup>19</sup> ASIC, 2018, Ibid

<sup>20</sup> Thorp et al, 2017, “Flicking the Switch: Simplifying Disclosures to Improve Retirement Plan Choices”. Available at <https://ssrn.com/abstract=2783113>

<sup>21</sup> Choice, 2017, “Submission to the Productivity Commission”, p. 8-10.

<sup>22</sup> Productivity Commission, 2018, ‘Superannuation Assessing efficiency and competitiveness’, p.13



considered within the context of chronically weak engagement with superannuation products generally, especially by young people who potentially have the most to lose from choosing inappropriate cover.<sup>23</sup>

### **Complex insurance offers reduce demand-side competition**

Complex insurance offerings compound the problem of weak demand side competition in the superannuation system<sup>24</sup> by increasing the overall complexity of choosing a superannuation product. The difficulty of making informed choices inhibits individual engagement, which is costly in several substantive ways. Firstly, in the form of individuals paying unnecessarily high fees.<sup>25</sup> The Productivity Commission enquiry found both that funds charging higher fees “typically do not deliver higher net returns”<sup>26</sup> and that the additional erosion of a 0.5% fee increase can reduce the retirement balance of a typical full time worker by 12% or \$100,000.<sup>27</sup> Secondly, by not consolidating unintended duplicate accounts which substantially reduce retirement balances, partially due to charging insurance premiums for cover which people often cannot claim due to multiple policy exclusions.<sup>28</sup> Thirdly, by not switching out of poor performing MySuper products.<sup>29</sup> By reducing the complexity of the choice of fund by simplifying the choice of appropriate insurance products, standardised terms contribute to the health of the superannuation system more broadly.

### **Minimum levels of cover need to be indexed**

There is also a role for mandatory minimum levels of cover that are appropriately indexed. Given that there are two main ways in which insurers respond to cost increases - increasing premiums and/or decreasing benefits - it is important to establish a floor on benefits in order to mitigate the creation of junk policies. The best way to define appropriate mandatory minimums and how they should vary over time is through an independent inquiry. Regarding set and maximum levels of cover, it is in members' interests for funds and insurers to have the flexibility to negotiate some level of tailoring of benefits in order to best reflect member characteristics. However, better information needs to be provided to members and the general public about how any policy is tailored so that people can understand if the policy is right for their needs and so there is greater accountability about the data used as part of trustee decisions.

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<sup>23</sup> Ibid, p.245

<sup>24</sup> Ibid, p.57

<sup>25</sup> Minifie J, Cameron T, Savage J, 2015, Super Savings. Available at <https://grattan.edu.au/report/super-savings/>

<sup>26</sup> Productivity Commission, 2018, 'Superannuation Assessing efficiency and competitiveness', p.153

<sup>27</sup> Ibid, p. 154

<sup>28</sup> Australian Lawyers Alliance, 2019, 'Submission to FSC'. Available at <https://www.lawyersalliance.com.au/documents/item/1436>

<sup>29</sup> Productivity Commission, 2018, 'Superannuation: Assessing Efficiency and Competitiveness', p.52

# Focus on Total and Permanent Disability (TPD) Terms, Definitions and Exclusions

## **TPD definitions must allow people to claim when they cannot work in a role they are reasonably qualified for**

Currently, the broadest allowable definition of TPD is that given in the SIS Act Regulations. It provides for cover if the claimant is “unlikely” to engage in “gainful employment” for which the member is “reasonably qualified” by “education, training or experience”. This “any occupation” definition is appropriate for superannuation cover as it is directed at protecting people who are forced to retire early from an occupation for which they are qualified, by replacing their lost opportunity to save for retirement. Any move away from this standard risks people slipping through the gaps and finding themselves without cover and no ability to work in a role for which they are reasonably qualified.

This relationship between being able to work in a role for which a person is reasonably qualified and an insurance benefit being paid is important. Departing from this standard gets away from the purpose of insurance in superannuation and further removes it from community expectations. It is reasonable that if a person has been paying for insurance for their entire working life, that that insurance will pay a benefit if they can no longer work in a role for which they are qualified. More restrictive standards take people away from this important relationship with their occupation and move them into a much more uncertain world of predicting their future capacity or arbitrarily punish them for not meeting a definition of employment.

### **Recommendation 2**

Standardise the definition of Total and Permanent Disability (TPD) to reflect the definition of permanent incapacity found in the SIS Act regulations.<sup>30</sup>

## **Clarity is needed about return to work probability assessments**

Over time and particularly following the global financial crisis, many TPD policies have begun to include narrower definitions of total and permanent disability. This narrowing was likely to mitigate the additional costs of a higher rate of TPD claims<sup>31</sup> and reduced fund performance, putting pressure on trustees to not excessively erode member balances. Among these was the move from “unlikely” to “unable” to work - which is a much more stringent definition as it requires the claimant to establish there is no possibility of their return to work.<sup>32</sup>

Further, the SIS Act Regulations definition of TPD has been interpreted by the courts in ways that reduce the scope for a successful claim. For example, *Shuetrim vs TAL life Ltd (2016)* interprets “unlikely” to mean “merely a remote or speculative possibility that an insured person will return to

<sup>30</sup> Superannuation Industry (Supervision) Regulations 1994 (Cth), regulation 1.03C

<sup>31</sup> Sydney Morning Herald, 2016, ‘Devils are in the detail in super life insurance’. Available at <https://www.smh.com.au/business/consumer-affairs/devils-are-in-the-detail-in-super-life-insurance-20160805-qqlnlk.html>

<sup>32</sup> Rice Warner, 2017, “Quarterly Group Risks Insights Bulletin: July 2017, p.2

such work” rather than “less than 50% chance”.<sup>33</sup> This does not conform with a standard legal ‘balance of probabilities’ interpretation. Balance of probabilities is a well-established and easily understood standard at law. It was also developed over time in recognition that in civil matters having a higher standard would be an unjust evidentiary burden to place on a person. Yet it is an injustice that we have now seen a more stringent criterion ingrained in life insurance contracts at the same time as many policies have also deliberately narrowed their definitions of TPD. Overall there has been a clear drift away from community expectations.

### **Recommendation 3**

Standardise the definition of the term “unlikely” in the SIS Act definition to mean “less than 50% chance” to ensure the interpretation of this term meets community expectations.

### **Activities of daily living tests are unfair and must be prohibited**

As noted in the PC inquiry<sup>34</sup>, there are substantial variations in TPD policies in terms of additional eligibility criteria and differing exclusions. Work status in the period up to the point of claim and the nature of the occupation determine the eligibility test used in many TPD policies. Claimants who are not employed in this period (often 6 or 12 months) or work in particular occupations are required to pass an “activities of daily living” (ADL) test which requires them to prove they are incapable of doing two of five specified activities. For example, to successfully claim a person needs to show that not only can they not work but are dependent on another person in performing basic “daily activities” like eating or using the toilet. This is a substantially more stringent test than the SIS Act “any employment” definition or even the narrower versions offered in some MySuper products.

The use of conditional eligibility criteria reduces the ability of individuals to make “apples for apples” comparisons of products and we concur with the PC inquiry that it is “contributing to inequitable outcomes for members across the superannuation system”.<sup>35</sup> While funds and insurers may justify such measures as a necessary evil to allow them to provide affordable premiums, their implementation often runs contrary to members best interests.

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<sup>33</sup> NSW Caselaw, 2016, “TAL Life Ltd v Shuetrim; MetLife Insurance Ltd v Shuetrim [2016] NSWCA 68”. Available at <https://www.caselaw.nsw.gov.au/decision/57034307e4b05f2c4f04c878>

<sup>34</sup> Productivity Commission, 2018, ‘Superannuation Assessing efficiency and competitiveness’, p.408

<sup>35</sup> Ibid.

### Case study – Sandra’s story

Sandra is very ill, with no prospects of ever returning to employment. Sandra relies heavily on a breathing machine. Sandra has cancer of the right lung; had a quarter of her lung removed four years ago, suffers from emphysema; asthma; and has a skin cancer in her upper right arm. Sandra’s partner is her carer. He is on Centrelink benefits. He had to stop work to look after her. They sold their house when she had the lung operation.

Sandra held two super products both with insurance policies for ten years. On one of the policies she made a successful claim that was paid out quickly. Her second insurance in super product however included a narrowed definition. Sandra made a claim and had to wait a very long time for a decision. Sandra put off operations waiting for this decision due to the expense.

The second insurer denied her claim as the insurer was not satisfied that Sandra could not perform two of the five activities of daily living: bathing or showering, dressing, moving from place to place including out of bed and into or out of a chair, eating or drinking, and using the toilet. The insurer had sent out a private occupational therapy expert to do an activities/daily living assessment. They said she can do all of the above with supervision.

*Source: Financial Rights Legal Centre*

For people working in intermittent, seasonal work or who have taken time out of paid employment to raise a family, policies with stringent conditional eligibility criteria can see people stripped of cover without their knowledge. Unless someone is cognisant of the fine print of a lengthy insurance policy, they are unlikely to know they have fallen foul of one of these restrictive policy terms. On the surface, they continue to be charged the same insurance premiums, but after six months and one day they may find their insurance has switched from good cover to junk insurance. Given the person is paying the same premiums and likely unaware of the restriction there is absolutely no fairness in this outcome. On this basis, we find that eligibility tests based on work status are not consistent with community expectations.

#### **Recommendation 4**

Prohibit the use of the more stringent eligibility criteria (including but not limited to Activities of Daily Living and Everyday Work Activities tests) for TPD insurance.

## **Payments linked to return to work initiatives harm consumers and must be prohibited**

Return to work initiatives are premised on the assumption that a significant proportion of TPD claimants will return to work within a few years of making a TPD claim. As evidence the issues paper points to a report produced by superannuation fund SunSuper. The assumptions and findings of this report need to be independently tested if the public is to have faith in this approach, particularly since it does not appear to be publicly available. Further research by an independent body is needed to establish the real rates of people re-entering the workforce. Even if the SunSuper evidence can be independently verified, the conclusion may not be to move away from our current approach of point in time assessments and lump sum payments. Involving insurers in 'return to work initiatives' will lead to an unmanageable conflict of interest. Given insurers' financial interest it is completely inappropriate for them to have any role in judging the likelihood of returning to work, this responsibility must always sit with independent medical professionals.

A related issue is the payment of TPD claims in instalments, rather than as a lump sum. Ostensibly this has reduced insurer costs and therefore people's premiums, but it may not be in member's best interests overall. There are a number of factors that go in to someone's rehabilitation. Chief among those factors is likely a degree of financial security and overall well being. Being subject to a constant system of assessment and reassessment in order to prove eligibility for an ongoing disability payment is very likely to restrict someone's rehabilitation prospects. The additional stringency of yearly eligibility tests has a demonstrated impact on the mental health of people.<sup>36</sup> A recent Beyond Blue survey found 50% of TPD claimants find making a claim damaging to their mental health.<sup>37</sup>

We are concerned that subjecting people to a never ending claims process will only compound the mental health issues people may already be experiencing. In a 2015 report, the Financial Rights Legal Centre documented the mental toll that lengthy claims assessment interviews have on claimants.<sup>38</sup> These effects are only likely to be compounded by repeated annual health assessments. From a mental health perspective, there is a perverseness in requiring a person to simultaneously have to remain positive about their recovery, while also having to demonstrate ongoing disability in order to qualify for payments. Overall, these payment structures may save insurers some money, but the mental toll on a person is tremendous.

### **Recommendation 5**

Prohibit policies which do not deliver TPD benefits as a lump sum as they have been shown to harm people who are receiving a benefit.

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<sup>36</sup> ABC News, 2018, "Sunsuper faces legal action over alleged 'improper' payments for disability benefits", Available at <https://www.abc.net.au/news/2018-06-03/sunsuper-insurance-members-sue-qld/9825324>

<sup>37</sup> ABC News, 2018, "Former insurance executive wants probe into treatment of customers with mental illness" Available at <https://www.abc.net.au/news/2018-03-14/former-insurance-exec-probe-treatment-customers-mental-illness/9542496>

<sup>38</sup> Financial Rights Legal Centre, 2016, "Guilty until proven innocent: Insurance investigations in Australia", Available at <https://financialrights.org.au/wp-content/uploads/2016/03/Guilty-until-proven-innocent.pdf>

## Cost of Standardisation

Funds and insurers have expressed concern that standardising terms may lead to a reduction in insurance benefits and/or a rise in premiums. For example, in its submission to the financial services royal commission, ASFA noted “the potential for existing insurance benefits to be reduced or limited through a change in definition”.<sup>39</sup> For example, creating new mandatory minimum levels of cover, may lead to higher premiums. Since the issue is arguably most acute with TPD terms, definitions and exclusions as these have narrowed substantially over time, we will focus on them. On the evidence<sup>40,41</sup> many current MySuper TPD insurance policy terms reduce the probability of a successful claim when compared to a policy which would simply apply the SIS Act definition and did not apply additional restrictions.

Fairer eligibility criteria through standardisation may see an impact on premiums, benefits and insurer profits. This impact will be due to people getting a good quality product rather than paying for something that is poor value for money. To ensure affordability and access to quality services in other uncompetitive markets for essential services (of which this is one) the Government has stipulated a level of service and given the regulator the power to establish a reasonable rate of return to the service provider (e.g. telecommunications). Subject to the independent inquiry we have called for, we may discover similar responses are required in this market. Properly accounting for equity, affordability, and community expectations needs to be the starting point of any analysis. To do otherwise will only tinker around the edges of the current problem.

Good policy in this area should be based on independent actuarial analysis, so that we can understand the true costs and benefits of the different methods of providing for people who cannot work due to disability. This would also be valuable as a stand-alone exercise. Mitigating premium rises may still be partially achieved from better fund and insurer understanding of fund member characteristics. This requires higher quality data collection and transparent release of information by stakeholders involved in making decisions about pricing risk.<sup>42</sup> Further, given that flexibility in terms of benefit levels may be limited to some degree by mandated minimums, it is crucially important to explore the question of what sort of mandatory minimum regime would best reflect community expectations of cover. This should follow from the principle that minimum levels of cover should meet community expectations and change over time in order to maintain relevance.

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<sup>39</sup> ASFA, 2018, “Submission to Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry — Round 6 Insurance in superannuation policy questions”, p.10

<sup>40</sup> Rice Warner, 2017, “Quarterly Group Risks Insights Bulletin: July 2017”, p.2

<sup>41</sup> Australian Lawyers Alliance, 2018, “Submission in response to Policy questions arising from Module 6”, p. 9-14.

<sup>42</sup> Productivity Commission, 2018, ‘Superannuation: Assessing Efficiency and Competitiveness’, p.363