Lawyers for the People

AUSTRALIAN LAWYERS ALLIANCE

Superannuation: Assessing Competitiveness and Efficiency

Submission to the Productivity Commission

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Protecting and promoting justice, freedom and the rights of the individual

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Who we are

The Australian Lawyers Alliance (ALA) is a national association of lawyers, academics and other professionals dedicated to protecting and promoting justice, freedom and the rights of the individual.

We estimate that our 1,500 members represent up to 200,000 people each year in Australia. We promote access to justice and equality before the law for all individuals regardless of their wealth, position, gender, age, race or religious belief.

The ALA started in 1994 as the Australian Plaintiff Lawyers Association, when a small group of personal injury lawyers decided to pool their knowledge and resources to secure better outcomes for their clients – victims of negligence. While maintaining our plaintiff common law focus, our advocacy has since expanded to criminal and administrative law, in line with our dedication to justice, freedom and rights.

The ALA is represented in every state and territory in Australia. More information about us is available on our website.[1]

[1] www.lawyersalliance.com.au.

Introduction

1. The Australian Lawyers Alliance (ALA) welcomes the opportunity to have input into the Productivity Commission's Stage 3 Inquiry *Superannuation: Assessing Competitiveness and Efficiency*. This submission makes some general comments on the impact of insurance premiums on retirement incomes and whether policy changes could improve default coverage.

The impact of insurance premiums on retirement incomes of both default cover and individually underwritten cover funded inside of superannuation

2. Default or 'opt out' insurance in superannuation is a very valuable resource for working-age Australians and helps to alleviate this country's chronic underinsurance problem. Properly regulated and sustainable default insurance cover in superannuation is indispensable.

3. Australian households are among the most indebted in the world, and the underinsurance gap means that working Australians and their families depend more than ever on default cover. That gap would be much larger if cover was not provided through super.

4. We see the value in default insurance every day, as our disabled clients receive insurance benefits that allow them to make ends meet and avoid falling into a debt trap as they struggle to cope on medical retirement.

5. It is essential that the right balance is struck between a sustainable, competitive industry and quality low-cost cover that addresses the underinsurance gap. It is clear that the industry has faced significant challenges in achieving that balance, including

by increasing premiums to make up for poor financial results during a post-GFC 'claims slump' and by toughening policy definitions.

6. It is encouraging to see that more recently, however, the industry has demonstrated that it is listening to community and regulatory concerns and is taking action to find the right balance, most notably through the Insurance in Superannuation Working Group (ISWG). The ISWG has focused on addressing account balance erosion, member engagement, product design and claims-handling issues. The ALA have made submissions to the ISWG on these topics.

7. We also support the decoupling of death and disability cover to enable greater flexibility for younger workers who require none or minimal death cover, and note that several funds have already reduced or ended default insurance for younger members who are less likely to have financial dependants or mortgage debt.

8. However, there is still much work needed and these areas for improvement are discussed below.

The prejudice members may suffer by auto-consolidation or auto-cessation

9. One area of concern is around any regulatory intervention to automatically consolidate members' duplicate super fund accounts. The ALA believes that automatic events that affect or remove insurance provided as a part of superannuation has the potential to dramatically reduce the utility of such insurance.

10. It is not good public policy to automatically consolidate into a fund that provides life or TPD insurance that is:

    (a) inferior in its terms, such as those with the sub-standard terms discussed above; or

    (b) less adequate in its quantum to the cover being relinquished.

11. The same principle applies to any automatic cessation of insurance in an inactive fund; that is, if auto-cancellation leaves the member with an inferior or less adequate cover than their prevailing fund, they are being inappropriately disadvantaged.

12. There are many circumstances in which contributions inactivity or low contributions activity occurs, such as: illness, pregnancy, extended leave, overseas work, seasonal work, underemployment and unemployment. In such situations, some policies provide for automatic consolidation or cessation of the policy, without adequate notice to the policy holder.

13. The ALA believes that any auto-consolidation or auto-cessation must be subject to a No Disadvantage Test. That will necessarily require a rating and comparison of definitions, and a system to ensure that a member being consolidated does not end up with reduced insurance coverage.

14. There must also be robust practices in place to notify policy holders of proposed auto-consolidation or auto-cessation, with practical information as to the risks of losing cover, to allow them to opt-out of any such automated event.

Policy changes that could improve default cover through superannuation: standard definitions

15. The ALA supports having default insurance as a part of superannuation. People in Australia are chronically underinsured, and default cover goes some way to remedying that problem. However, there is a need to tighten regulation so that the insurance provides meaningful benefits to policy holders. We believe that standard definitions, with an obligation on insurers to notify policy holders where their policies diverge from these definitions, would be the best way to improve default

cover and ensure that meaningful coverage is available to policy holders who need to make a claim.

16. Below are a selection of the problems that the ALA believes would be remedied by standard definitions.

Restrictive definitions

17. The ALA has called for the application of standard TPD definitions in line with the *Superannuation Industry (Supervision) Act 1993* (Cth) (SIS Act) and the *Superannuation Industry (Supervision) Regulations 1994* (Cth) (SIS Regulations)[2] to ensure that consumers have access to fair coverage.

18. Harsh TPD definitions that deviate from the SIS requirement of permanent incapacity have resulted in some insurance products that will not pay out genuine claims. There is a need for standard definitions in line with the SIS Act and Regulations to be introduced to remedy problematic definitions and the resulting reduction in coverage.

Unlikely vs unable

19. For example, we have been particularly concerned with the use in different definitions of 'unlikely' and 'unable'.

20. 'Unlikely' has been interpreted by Australian courts to require a consideration of 'the real world' – namely, market conditions – in assessing whether the person is unlikely to return to work given their injuries or illness.

[2] See the definition of 'Permanent Incapacity' provided for in reg1.03C of the *Superannuation Industry (Supervision) Regulations 1994* (Cth): 'a member of a superannuation fund or an approved deposit fund is taken to be suffering permanent incapacity if a trustee of the fund is reasonably satisfied that the member's ill-health (whether physical or mental) makes it unlikely that the member will engage in gainful employment for which the member is reasonably qualified by education, training or experience'.

21. By contrast, insurers argue that 'unable' is a medical assessment without consideration of the 'real world'. For instance, it is possible to argue that even a quadriplegic is theoretically capable of work and may not satisfy an 'unable' definition even though they would not be able to obtain work in the competitive labour market.

22. AustralianSuper, with over one million members, was one of the first large funds to change its TPD definition to remove the word 'unlikely'. It now requires claimants to demonstrate that they are 'incapable of ever engaging in any occupation for which [they are] or may become reasonably suited by education, training or experience'.

23. The threshold 'incapable of ever engaging' is much higher than 'unlikely', the latter of which is found in the SIS 'Permanent Incapacity' definition. Many seriously incapacitated claimants with no genuine prospect of future employment would find the former threshold difficult or impossible to meet.

24. The NSW Court of Appeal recently considered the 'unlikely' TPD test and found that 'a real chance that a person will return to relevant work, even if it is less than 50 per cent, will preclude an Insured Person being unlikely ever to return to relevant work'.[3] Surely that test is sufficiently onerous.

Retraining clauses

25. Another example is the introduction by many funds of retraining clauses that would mean that a manual labourer who can never again do physical work due to an orthopaedic injury will not meet the TPD threshold if, theoretically, s/he could retrain and work in a call centre, even if no employer would give her or him such a job in the real world.

[3] *TAL Life Ltd v Shuetrim; MetLife Insurance Ltd v Shuetrim* [2016] NSWCA 68 at [89].

Ongoing care

26. Another example is found in the current MTAA Super/MetLife policy which contains the following definition for regular and ongoing care. It means that the person:

> 'a. Is under the regular and ongoing care of a medical practitioner who has given a clear prognosis that the Injury or Illness will continue throughout the life of the Covered Person (including after the expiry of the cover and the commencement of retirement) without any prospect of an improvement which would lead to a return to work (whether or not for reward) in any capacity; and
>
> b. Is complying with reasonable medical advice and treatment; and
>
> c. Has, in our opinion reached the maximum level of medical improvement possible for that Covered Person based on their Injury or Illness.'

27. This is perhaps the most severe departure from the SIS definition, which determines eligibility by reference to a member's education, training and experience.

28. The chances of a claim being admitted are deleteriously low due to the difficulty a claimant will have procuring such unequivocal medical opinion, which effectively requires that a doctor assure against future improvement. Few doctors would provide such a pessimistic message to their patient.

Limited cover

29. Another example is that many members' death or TPD cover will exclude a claim arising from a condition that existed prior to the commencement of cover, or only assess the member under an Activities of Daily Living (ADL) definition. That may occur where the insurer deems that the member was not working sufficient hours or was working on a restricted basis, by reference to an 'at work' or 'active employment' test in the relevant policy.

30. A member does not usually find out about the application of the exclusion until their claim is declined on that basis. Moreover, despite reduced coverage such limited cover does not attract a lower premium. That is because neither funds nor insurers know which group members will be deemed to have limited cover until after a claim is lodged.

31. That is clearly inadequate:

    (a) Firstly, those members with coverage that excludes pre-existing conditions or who are only covered for ADL should be paying a much lower premium to reflect the vast inferiority of their coverage. By charging the standard premium funds and insurers are improperly eroding their account balances and that cannot be consistent with s52(7)(c) of the SIS Act which states that a trustee must 'only offer or acquire insurance of a particular kind, or at a particular level, if the cost of the insurance does not inappropriately erode the retirement income of beneficiaries'.

    (b) Secondly, members with such inferior cover ought to have certainty regarding the insurance cover they hold to enable them to determine whether such cover is adequate and if not to seek additional or alternative cover.

32. Blanket underwriting, whereby the same coverage is provided to all members regardless of their personal circumstances, is not the problem per se. It is too costly to individually underwrite millions of policy holders. However, 'at work' or 'active employment' definitions vary widely from one policy to another, and minimum standards should be developed to provide for full cover as long as members meet minimum work attendance.

33. We propose that full cover should be granted where either of the following has occurred:

    (a) A certain qualifying period of unrestricted employment has passed; or

(b) A member's compulsory super guarantee contributions made to the fund by the employer is above a threshold set by the fund/insurer.

34. Neither of the above are burdensome administratively as funds obviously have that data on their members' contribution periods and amounts ready to hand. Using that data, funds and their insurers could determine the scope of cover for each member, and clearly disclose same to them in their periodical membership statements. It is submitted that the above approach is workable and reasonable: if after a qualifying period of employment a pre-existing condition has not caused a member to cease work, or within that qualifying period they are working sufficient hours to attract a certain level of super guarantee contributions, then any such pre-existing condition's effect on risk is much diminished. The insurer ought to recognise that by providing full coverage.

The implications for members and for the industry

35. These inadequate products will result in the denial of claims by genuinely incapacitated members who would have been entitled to a TPD benefit under a traditional definition, which will in turn attract media attention and heightened public scrutiny of the feasibility of default insurance in superannuation.

36. Some funds have claimed that their definitional changes are merely intended to clarify the TPD definition. However, these changes have not been accompanied by any 'no-disadvantage' guarantee to members.

37. It is pleasing to see that some funds, such as CBUS, have resisted a departure from the SIS 'Permanent Incapacity' definition, by retaining the 'unlikely' definition. The fact that such definitions are being retained by some funds supports the viability of doing so across all funds.

Recommendations

The ALA makes the following recommendations relating to insurance in superannuation:

- Insurance premiums' impact on retirement income can be mitigated by ensuring that premiums adequately reflect the level of cover being offered to policy holders from the outset, rather than seeking to reduce coverage at the point of claim by relying on exclusions such as pre-existing conditions;

- Auto-consolidation and auto-cessation should be subject to a no-disadvantage test, and should never occur without ensuring that the policy holder is aware that automatic consolidation or cessation is about to occur, what the implications of such an automated event might be, and how they can avoid the automated event from occurring; and

- Standard definitions should be introduced into all insurance provided through superannuation, with an onus to be placed on the insurer/superannuation fund to inform policy-holders of any deviations from standard definitions, and how this might affect their coverage as compared to what they would be entitled to if the standard definitions applied.