



Law Council
OF AUSTRALIA

Legal Practice Section

26 April 2019

Division Head
Retirement Income Policy Division
Treasury
Langton Cres
PARKES ACT 2600

By email: superannuation@treasury.gov.au

Dear Division Head

Submission – Universal Terms for Insurance within MySuper

1. In this letter, the Superannuation Committee (**the Committee**)¹ of the Law Council of Australia responds to the Government's Issues Paper entitled 'Universal terms for insurance within MySuper - Taking action on recommendation 4.13 of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry' (**Issues Paper**).
2. As recorded in the Issues Paper, Commissioner Hayne recommended:
 - that Treasury, in consultation with industry, determine the practicability of legislating universal key definitions, terms and exclusions for default MySuper group life policies; and
 - that the review should also consider the merits of prescribing:
 - higher minimum coverage for life insurance than is currently provided for by the *Superannuation Guarantee (Administration) Regulations 2018*;
 - minimum coverage for permanent incapacity insurance;
 - maximum coverage for life and/or permanent incapacity insurance; and
 - a fixed level of coverage for life and/or permanent incapacity insurance so as to set a standard amount of default insurance across all MySuper products.
3. With great respect to the intention underlying the recommendations, the Committee considers that none of these suggestions is feasible given the context in which trustees must operate, when viewed from the perspective of the existing legislative

¹ The Law Council of Australia is a peak national representative body of the Australian legal profession. It represents the Australian legal profession on national and international issues, on federal law and the operation of federal courts and tribunals. The Law Council represents 60,000 Australian lawyers through state and territory bar associations and law societies, as well as Law Firms Australia.

regime applying to superannuation trustees in relation to insurance in superannuation. The existing legislative regime would need to be radically altered before these suggestions could be adopted. The rest of this letter sets out why the Committee considers this to be so.

Insurance covenants

4. A superannuation trustee is subject to a variety of insurance-specific covenants under section 52(7) of the *Superannuation Industry (Supervision) Act 1993 (SIS Act)*. Those covenants are in the following terms:
 - (a) to formulate, review regularly and give effect to an insurance strategy for the benefit of beneficiaries of the entity that includes provisions addressing each of the following matters:
 - (i) the kinds of insurance that are to be offered to, or acquired for the benefit of, beneficiaries;
 - (ii) the level, or levels, of insurance cover to be offered to, or acquired for the benefit of, beneficiaries;
 - (iii) the basis for the decision to offer or acquire insurance of those kinds, with cover at that level or levels, having regard to the demographic composition of the beneficiaries of the entity; and
 - (iv) the method by which the insurer is, or the insurers are, to be determined.
 - (b) to consider the cost to all beneficiaries of offering or acquiring insurance of a particular kind, or at a particular level;
 - (c) to 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; and
 - (d) to do everything that is reasonable to pursue an insurance claim for the benefit of a beneficiary, if the claim has a reasonable prospect of success.
5. These covenants avoid detailed prescription. They assume that the trustee is best placed to investigate and understand the insurance needs of fund beneficiaries and they require the trustee to formulate an appropriate insurance strategy accordingly. In doing so, the trustee is specifically required to have regard to 'the demographic composition of the beneficiaries' of the fund.
6. When one considers the differing memberships of various Australian Prudential Regulation Authority (**APRA**)-regulated superannuation funds, it is obvious that key definitions, terms and exclusions that may be appropriate for the members of one fund may not be appropriate for the members of another fund. The existing law recognises this reality. It does not purport to impose uniformity for uniformity's sake.

MySuper

7. The insurance covenants set out above apply in relation to MySuper members and also in relation to choice members. The rules that are specific to MySuper members also need to be considered.

8. In this respect, the core characteristics of a MySuper product are set out in section 29TC of the SIS Act. By section 29TC(1)(b), 'all members who hold a beneficial interest of that class in the fund are entitled to access the same options, benefits and facilities except to the extent that a benefit is provided by taking out risk insurance' (emphasis added). The emphasised words reflect the considered decision of past policymakers that the prohibition on differential treatment, otherwise so central to the concept of MySuper, should not be adopted, to the same extent, in relation to insurance.
9. The prohibition on differential treatment applies strongly in relation to investments – both as between funds (the investment strategy must be diversified or it must be lifecycle) – and also within a MySuper product, as amounts must be 'attributed to members in relation to their beneficial interest of that class in the fund in a way that does not stream gains or losses that relate to any assets of the fund to only some of those members, except to the extent permitted under a lifecycle exception': section 29TC(1)(c).
10. The prohibition on differential treatment also applies strongly in relation to fees: Division 5 of Part 2C of the SIS Act.
11. However, a different approach was taken to insurance. In addition to the exception in section 29TC(1)(b), a requirement was introduced to provide permanent incapacity benefits and death benefits by taking out insurance: section 68AA. However, the level of insurance cover was not prescribed. Further, a trustee was allowed to set reasonable conditions to which the provision of permanent incapacity benefits and death benefits would be subject: section 68AA(2) – (4). In deciding whether to set any such reasonable conditions, the superannuation trustee would have to think about, and comply with, its insurance covenants as set out earlier. Many trustees have relied on this exception to exclude insurance cover for members in casual work. This is very often an eminently sensible decision to take.
12. The requirement under the Superannuation Guarantee legislation to provide a minimum amount of death cover was, at the same time, also made subject to the trustee's ability to set reasonable conditions.
13. Again, the regime outlined above reflects the considered decision of past policymakers that the prohibition on differential treatment, otherwise so central to the concept of MySuper, should not be adopted, to the same extent, in relation to insurance.

Discussion

14. The Issues Paper does not identify any flaw in the decision-making of past policymakers. If anything, the Issues Paper appears to confirm the merits of that decision-making. It refers repeatedly to the 'tailoring' of insurance cover (to the needs of the particular fund's membership) that has been both accommodated and required by the existing legislative regime.
15. The Issues Paper refers briefly to some (but not all) of the legislative requirements and goes on:

Beyond complying with these requirements, trustees have discretion to determine the insurance offering provided via their MySuper product. This includes the terms and conditions, any exclusions, and the level of coverage. This discretion has

resulted in a broad variation in the default insurance coverage being provided to MySuper members.

16. The Superannuation Committee does not agree with the premise of this statement. It is not the case that a superannuation trustee enjoys discretionary decision-making powers in relation to insurance. As explained earlier, a trustee's decision-making in relation to insurance is affected by a range of general covenants and insurance-specific covenants. A trustee's decision-making in relation to insurance is not a matter of 'discretion' in the usual sense of the word.
17. The way the matter is presented in the Issues Paper suggests that superannuation trustees have no particular boundaries when considering the insurance cover they will make available to their members.
18. The Superannuation Committee suggests that the much more likely explanation for the 'broad variation in the default insurance coverage being provided to MySuper members' lies in superannuation trustees investigating and understanding the insurance needs of fund beneficiaries and then formulating an appropriate insurance strategy accordingly.
19. The Issues Paper also refers to the efforts of the Insurance in Super Working Group (**ISWG**) in a manner that suggests that the ISWG may have been (in the view of the author of the Issues Paper) tardy in dealing with an issue – standardisation of terms – that should have been dealt with and resolved at an earlier time. However, the Committee considers that it is just as plausible that the ISWG has been unable to produce anything tangible on this topic because the topic is vexed and does not yield obvious or easy solutions.
20. And yet the Issues Paper does recognise, in other places, that variation in insurance coverage may have more to do with trustees complying with their duties than with trustees exercising a discretion. Referring to some definitions of Total Permanent Disability (**TPD**) being 'narrower than the SIS Act definition allows for', the Issues Paper states that 'they may more closely reflect trustees' broader obligations to members, such as under the insurance covenant contained in section 52(7) of the SIS Act'. The Committee respectfully suggests that this is likely to be correct.
21. The Superannuation Committee does suggest that the quest for greater understanding of the details of insurance cover may be a little unrealistic. Are members and prospective members really going to better understand the insurance made available if superannuation trustees are, for example, required to use the word 'unlikely' in their TPD definitions, and prohibited from using the word 'unable'?
22. The Superannuation Committee can readily understand the factors that led Commissioner Hayne to make the recommendations he did and to ask the questions he did. However, as stated, and with great respect, the Committee considers that none of the suggestions is feasible given the context in which trustees must operate.

Contact

23. The Committee would welcome the opportunity to discuss its submission further and to provide additional information in respect of the comments made above. In the first instance, please contact:
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Yours sincerely

A handwritten signature in blue ink, appearing to read 'Jonathan Smithers', with a long horizontal stroke extending to the right.

Jonathan Smithers
Chief Executive Officer