19 January 2017

Budget Policy Division
Department of the Treasury
Langton Crescent
PARKES ACT 2600

Email **prebudgetsubs@treasury.gov.au**

Dear Sir/Madam

Pre-Budget submission (2017-2018)

The Actuaries Institute presents this pre-Budget submission primarily to help maintain the sustainability and efficiency of the superannuation and insurance sectors. By encouraging the public to protect itself against various financial risks, the ongoing pressure on the cost of social services can be reduced. This outcome is consistent with the Government's goal "to sensibly and responsibly restrain government expenditure" whilst continuing to "provide the services the community needs and expects". (Minister for Small Business Michael McCormack 9/12/2016)

To pursue those aims, whilst meeting community expectations, the Institute proposes the Government quickly adopt the policy approaches outlined below.

Encouraging retirement income streams (CIPRs)

The Institute released a research report "For Richer, For Poorer" in September 2015 that outlined the financial risks facing future retirees based on their current age and wealth profile. Many of those risks can be partially managed by the introduction and promotion of Comprehensive Income Products for Retirement (CIPRs). CIPRs are an outworking of the FSI's investigation of the efficiency of the superannuation system. The goal of protecting retirees against longevity risk is supported by the Institute.

The introduction of CIPR-style products should deliver greater income security and protection throughout retirement. The Government is encouraged to move quickly to establish a CIPR framework and remove any social security means testing and taxation policy settings that constrain CIPR product development and consumer take-up.

Rationalisation of life insurance legacy products

The life insurance market has experienced some consumer backlash recently, due in part to outdated policy terms and conditions (including health definitions). The FSI had recommended that a mechanism be introduced to facilitate the rationalisation of life insurance legacy products (Rec 43). This matter has been an issue for considerable time now despite general acceptance that the proposal has merit. The FSI recommended action to resolve the situation and the Government has accepted that recommendation.

In a recent APRA parliamentary submission (PJC Corporations & Financial Services, 30 November 2016), it opined:

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"The contract between a life insurer and a policyholder is very long term; it is difficult to renegotiate the terms of the product and the insurer must be ready and able, in some cases, for decades, to fulfil its obligations under the contract. APRA therefore continues to support the Financial System Inquiry (FSI) recommendation regarding the rationalisation of legacy life products. Legacy products become more complex and expensive to administer over time and are prone to problems such as the use of outdated medical definitions. There are a range of legal, consumer and tax issues that inhibit an insurer's ability to update legacy products. Introducing a rationalisation mechanism, as recommended by the FSI, would help address this issue; this, however, requires legislative change."

We agree with APRA's view and therefore urge Government to pursue legacy product rationalisation more vigorously. Instilling greater public confidence in the life insurance sector will potentially boost demand for risk products with the consequent effect of reducing social service payments.

Climate Change and Natural Disaster Funding

Based on expert scientific findings, the Actuaries Institute recognises that climate change is expected to have major environmental, economic and social impacts, and poses a serious risk to the industries that actuaries advise. We estimate an annual natural peril cost to Australia of $11 billion, of which only 40% is insured. This figure excludes public assets, but does include the cost of intangible losses such as mental health and family violence as a result of natural disasters.

Accordingly, the profession urges the Government to support policies to improve resilience against natural disasters and to design funding mitigation and adaptation measures supported by comprehensive cost benefit analyses. The Institute's view is that a timely investment to mitigate the potential impacts of climate change will protect future budgets from significant adverse effects to the revenue.

The Institute is disappointed with the Government's recent decision not go to ahead with the $200m p.a. disaster resilience fund proposed by the Productivity Commission in its 2015 final report. The annual outlay can dramatically reduce the economy wide costs of increasingly intense climactic events. We recommend the funding decision be reviewed.

In addition, the Institute encourages the Government to include estimates of the future costs of natural disasters to its budget in the Statement of Risks. The "Statement of Risks" should include both expected costs and also costs at different annual return intervals. This provides transparency and encourages planning for the expected cost of natural disasters.

Should you wish to discuss any aspects of this submission or make arrangements for a meeting with Institute representatives please contact Chief Executive Officer of the Actuaries Institute, David Bell on (02) 9239 6106 or by e-mail david.bell@actuaries.asn.au.

Yours sincerely

J. A. Lyon

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President