CORPORATE SUPERANNUATION ASSOCIATION Inc.

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28 May 2018

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

Email: superannuation@treasury.gov.au

Dear Sir or Madam

Treasury Laws Amendment (Protecting Superannuation) Bill 2018: Exposure Draft

We refer to the invitation to comment on the draft legislation issued on 8 May 2018.

The Corporate Superannuation Association

Established in 1997, the Association is the representative body for large corporate not-for-profit superannuation funds and their employer-sponsors. The Association now represents a total of 21 funds controlling $51 billion in member funds, held in a total of some 274,000 individual accounts. Of these funds, 13 have outsourced trustee services but maintain significant employer interest through policy committees. In general, these funds are sponsored by corporate employers, with membership restricted to employees from the same holding company group, but we also include in our membership two multi-employer funds with similar employer involvement and focus. A number of our funds have defined benefit divisions.

Some of the smaller funds have their place in the pension fund structures of international groups, hence play an important role in the care and welfare of the worldwide workforces of these groups.

General comments

We have major concerns with the insurance aspects of the proposals.

In addition, we provide comment on the proposals regarding fees.

Insurance issues

Background: insurance in our funds

We represent funds where the employer-sponsors have a well-established pattern of using superannuation and related insurance against death, and temporary and permanent disability as a benefit adapted to the needs of the employers' particular work forces. We have in our membership funds that serve the employees of diverse companies involved in enterprises such as energy, extraction, shipping, communications and delivery, and insurance.

These work forces include some members with particularly hazardous occupations where insurance coverage requires specialist group cover. This is typically negotiated on better terms than would be available under more general group coverage, given the relative homogeneity of the work force and the known experience within that work force.

In addition, where the occupations are not particularly hazardous, the employers and funds have negotiated insurance arrangements that take advantage of experience in the relevant work forces to secure favourable terms. Further, the insurance arranged in this way often provides superior cover, with the facility of taking into account special locations and working conditions. A number of employers have also negotiated income protection cover on favourable terms.

In many cases, the employers subsidise these arrangements, directly or indirectly, with some providing the cover without charge to the employees' accounts and some providing it without charge to the employee even if the particular employee has in fact exercised choice to join an external fund. This will often provide a superior level of cover (free to the employee) to that available in the choice fund, and does not erode account balances.

Low balance members and members under 25

New employer-sponsored members of our funds typically begin their membership with no account balance (regardless of whether an external roll-over is received, as this cannot occur on day 1 when establishment of membership is tied to employment), and would therefore be excluded from coverage unless they opt in, until their account balances reached the $6,000 level.

The removal of automatic coverage for the first year or two of employment, and for a significant number of years for those under 25, would not be in the best interests of these members:

- They would miss out on valuable coverage against death and disability, and in many cases income protection.
- Many are in high risk industries and will have dependents.
- This cover, in many cases, would have been available without cost to the member.

Administrative issues related to insurance

There are administrative issues that arise in respect of the proposals, which would not work in the best interests of the membership as a whole. These are outlined below.

Renegotiation of group insurance terms

Insurance arrangements of our member funds are currently negotiated on the basis that when a member starts employment, insurance cover commences. If the proposals are implemented, there will need to be revised arrangements to exclude under 25s, new employees and inactive accounts. These exclusions will be sufficiently significant that new insurance contracts will need to be negotiated. The likely result is that insurance premiums will increase significantly across the entire membership, including for the under 25s who opt in. The probable increase would result partly from the need to negotiate out of the usual cycle in a tightening market, and partly from the removal of a large cohort from the insured population.

Commencement of cover

The new conditions on commencement of insurance would cause confusion, with members uncertain of whether or not they hold cover at a point in time. Currently the approach is unambiguous, with cover that generally commences as soon as an employee commences work. With the introduction of a $6,000 account requirement, the determination of the point at which cover commences becomes difficult, given that account balances can vary with investment performance, contribution inflows and any account costs.

Availability of automatic cover for those who have reached age 25 or $6,000 balance trigger point

The provision of cover for a new employee who has started work, without further evidence of health, is a valuable standard feature of death and disability and income protection insurance group contracts. The passing of time from commencement of work to the starting of insurance cover could result in the need for further evidence of health for the member requiring insurance. This could result in denial of cover or increased costs for the relevant members and would then operate as a significant barrier to cover for a member. Arguably, if insurers did require underwriting at this stage, this would effectively operate as a permanent extension of the "opt in" requirement. This is not a desirable outcome for members.

We strongly urge that the proposals to change these members' arrangements to default "opt in" be reconsidered in light of the above.

Inactive accounts over $6,000

Despite the "opt-in" provisions, there is increased risk that members with higher account balances could inadvertently lose their insurance cover because of a period of contribution inactivity. Reinstatement could then be problematic, including risk of underwriting problems.

Funds have reported that it is not unusual for there to be a two-year period of account inactivity, followed by further contributions.

It is recommended that a period longer than 13 months be set as the parameter for "inactive" accounts.

Members who are automatically covered at employer's expense regardless of fund choice

It is not in the interests of those members identified in the draft legislation (under 25s, members with low balances and inactive members) to be excluded on a default basis from their employer-sponsored funds in the following circumstances:

The employer is bearing the cost of the premiums as a separate cost from the contracted or compulsory superannuation contributions, i.e. the insurance cover is an additional benefit.

We urge that the Bill should include an exception for employer-paid premiums regardless of the member's age or account balance.

Cover for those whose premiums are paid from member account

In some cases, premiums (death and disability and/or income protection) are paid by members.

As in the situation where the employer pays or funds the premium directly, the automatic removal of the insurance protection may work significantly to the employee's disadvantage, particularly where the employer support aims to provide cover for particular risks or circumstances. There is, again, the additional risk arising from the need to seek coverage elsewhere, with attendant increased costs, potential underwriting, and reduced quality and suitability of product to the employee's circumstances.

Please let us know if we can assist with further detail about insurance arrangements. Our funds have wide experience in this area, and wish to see their members well protected at minimum cost.

Removal of exit fees and low balance protection

In relation to these matters we have the following comments.

Exit Fees

We acknowledge the intent to remove barriers to consolidation of accounts. However, we note that the costs of operating a fund (of which paying benefits is a component) is not reduced by removing exit fees. In fact costs may actually increase if there is no deterrent, in the form of a fee, to requesting multiple payments. So if no fee can be charged based on the activity of paying a benefit (or a partial withdrawal or a release of monies to the ATO to cover Division 293 tax) then this cost has to be shared across the members of the fund. Whilst the objective of the measure is clear, the effect is going to be to increase costs on other members who are not moving their money around.

Low Balance Fee Caps

One of our funds, with about 15,000 members, has costed this measure as currently proposed at around $100,000 per annum, representing at least a 20 fold increase on the historic member protection costs.

Our issues with the fee limit, as currently proposed, are:

- how it is proposed to be applied; and
- the fees to which it is to be applied.

Application of the fee limit

Calculating the fee limit on the balance at the start of the period gives rise to significant potential to "game" this fee limit. For example:

A member has a \$10 balance at the start of the period meaning that fees for the next 6 months are limited to 1.5% x \$10 = \$0.15.

Then the member brings in a rollover of \$1 million on the 2nd day. However, under the proposals, beyond the 15 cents no investment fees can be charged for the next 6 months. Then the member can repeat the process through a rollover to another fund and avoid fees indefinitely, by starting a new account late in each period and rolling money from fund to fund immediately after the start of each period.

If a fee cap is to be applied we recommend it should be designed to operate reasonably consistently with the historic member protection structure, the features of which were broadly that the cap was applied:

- at the end of the review period (i.e. once per year);
- based on the balance at the end of the period; and
- as a rebate to the fees charged.

Investment fees and indirect costs

Inclusion of investment fees and indirect costs under the capping is problematic as members can select against the fund and choose high risk, high return options for which they don't pay.

Again it needs to be remembered that the costs that are being limited for certain members do not disappear, but are met by the other members.

Please let us know if we can assist with further background on these issues.

Yours faithfully

Bruce McBain
Chief Executive Officer
Corporate Superannuation Association