4 June 2018

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

Email: superannuation@treasury.gov.au

Dear Sir/Madam,

SMSF ASSOCIATION SUBMISSION ON PROTECTING YOUR SUPER PACKAGE

The Self Managed Super Fund Association (SMSFA) welcomes the opportunity to make a submission on the Government's Protecting Your Super package. Ensuring that Australians' superannuation is preserved for retirement is essential to the success of Australia's retirement income system. The SMSFA supports the proposals in the package as an effective part of this process.

Our submission draws attention to the fact that there are a significant number of SMSF members who retain large superannuation fund accounts, often for the purpose of maintaining insurance policies. We understand that up to 40 per cent of SMSF members potentially have large superannuation fund accounts, where many of them hold an insurance policy. These accounts are likely to have a very low balance, often under $6000, or potentially be deemed inactive if they only receive sporadic contributions to pay for insurance premiums. This means that SMSF members holding insurance in large superannuation funds may be adversely affected by the proposed legislation. Accordingly, we recommend some minor amendments to the draft legislation to reduce the potential impact of having insurance cancelled. These issues are explored in detail below.

Fees charged to superannuation members

Prevention of administration and investment fees exceeding 1.5 per cent of accounts with less than $6,000 for a six month period.

We support the proposal and encourage the cap to be reduced as the superannuation system continues to evolve. As technology and efficiencies improve there will be scope for administration and investment fees to fall below the current cap of 3 per cent for a 12 month period. This will further benefit those members who face disproportionally high fees compared to their balances.

Prevention from charging exit fees on all superannuation products.

The Association is supportive of measures that give individuals more choice and flexibility about where they want their superannuation to be held and invested. Banning exit fees will allow individuals to have the freedom to rollover or consolidate their superannuation to a fund of choice without being affected by fees that may impede their decision making.

We encourage the Government to review the transaction fees associated with buy-sell spreads at an appropriate time to ensure that these fees are not increased to cover the loss of exit fees.

Insurance for superannuation members

Prevention from providing opt out insurance to accounts of new members aged under 25 years, all accounts with balances below $6,000, and all inactive accounts unless a member has directed otherwise.

Insurance in superannuation is a policy issue that the SMSFA is concerned with, especially regarding the provision of default life insurance to young superannuation fund members on an opt-out basis. Our concern stems from the reduction in member account balances of young superannuation fund members caused by insurance premiums that may not meet their requirements.

The SMSF Association supports the provision of insurance through superannuation where it meets member needs. Where members are not able to work until retirement age due to disablement or death, insurance provided through superannuation is an important source of income for the fund member and their family. However, we have concerns that the current arrangements are inappropriately targeted and result in the erosion of member balances early in life.

The current practice of large superannuation funds is to issue new members of their fund with default total and permanent disability insurance (TPD), life insurance and in some circumstances income protection insurance. MySuper products are required to automatically offer members these polices on life and TPD polices on an opt-out basis. While this approach may overcome cognitive biases of disengaged superannuation fund members to not insure against income risk, it also comes with the downside of eroding retirement income and poorly targeting the insurance needs of fund members.

We are most concerned about the default provision of life insurance policies to young superannuation fund members as opposed to TPD cover. We believe that for employees of any age, TPD cover is an appropriate use of superannuation as it can play an important role in providing income if a young worker suffers permanent disablement early in life. However, it is less likely that a young superannuation fund member requires life insurance to insure against financial risks associated with their death.

Life insurance provides protection against risk of financial loss that would result from the death of the insured individual. The financial risks life insurance seeks to protect against include providing the deceased's family financial resources for mortgages, expenses of raising children and maintaining a standard of living for the deceased's dependants. It is less likely that a superannuation fund member holding life insurance early in their careers need to insure against these risks. However, default life insurance is a feature of APRA-regulated superannuation funds for new members, including those early in their career. We believe that this is inappropriate targeting of life insurance and the associated premiums reduce retirement savings.

Further, younger superannuation fund members are likely to have multiple accounts as they work in various jobs early in their career or undertake a combination of part-time work and study. This means that they can often have multiple life insurance policies being funded from their compulsory superannuation. Australian Taxation Office superannuation account statistics show that for the 2015-16 income year:

- 32.4% of people aged 18 to 25 have two or more superannuation accounts, and
- 44.2% of people aged 26 to 30 have two or more superannuation accounts.

These fund members, who are often the most disengaged from their superannuation due to retirement being a long way off, are potentially having their retirement savings eroded by multiple life insurance premiums that do need meet any of their current financial needs.

Preventing life insurance premiums from eroding the retirement savings of younger works will have a number of benefits:

- Retirement savings will be preserved through reduced premium payments from superannuation and reduced administrative costs benefitting fund members as investment returns compound over time.
- Confidence in superannuation will be improved for young people as their superannuation savings are not reduced by unnecessary insurance premiums.

The Association has previously called for life insurance to be an 'opt-in' product for people of under 30 years of age. We understand that at around age 30 people begin to consolidate their superannuation accounts making it less likely they will have multiple insurance policies eroding their retirement savings. Age 30 also aligns with when the Lifetime Health Cover penalty takes effect.

We are also supportive of age 25 as an appropriate age.

A new account with a member under 25 years old

We would encourage the Government to extend this proposal to existing accounts where the member is under 25 years. This would ensure that the existing generation of young members are not disadvantaged when they have more than $6,000 in superannuation.

Existing superannuation providers could supply a notification form allowing members the opportunity to declare that they wish to 'opt-in' to their continuing superannuation insurance.

Alternatively, this notification could be for 'opt-out' and at the very least provide a further opportunity for engagement with superannuation for young members.

Elections for insurance on inactive accounts

The SMSFA supports a written election for insurance to continue within an inactive account.

We note that it is a common practice for many individuals with an SMSF to also have a secondary APRA-regulated fund account which provides them with insurance. This is done for two key reasons:

- To access group insurance policies provided through large superannuation funds which are often cheaper than individual policies.

- To retain legacy insurance policies which may offer better benefits or lower premiums than new policies, especially for older members.

These individuals consider the SMSF to be their primary superannuation account and therefore direct their contributions and roll-overs to their SMSF. Where required they may orchestrate a rollover of funds from their SMSF to their APRA fund to pay for insurance premiums and administration fees to retain their insurance policy.

Under the proposal the APRA-regulated fund would be considered inactive if no contribution or rollover was received, yet it still may be considered active for the purposes of the individual. The SMSFA would be concerned if insurance was closed for these accounts because members have not checked their mail or correspondence, especially those for who rely on insurance held in an APRA fund separate to their SMSF.

Typically, those affected in this situation would be more engaged with their superannuation and may need to contribute at least once a year to facilitate insurance payments which would mitigate this risk, although this will not completely prevent unintended consequences.

The SMSFA therefore proposes that this election be 'opt-out' for those over the age of 25. We see the risk of an individual losing insurance when it is needed, greater than the erosion of superannuation. The notification from trustees should continue to be provided to members on inactive accounts until they receive a reply. This proposal is based on the premise that 'opting-in' is a significant shift in policy that could severely impact SMSF individuals and their families that may be depending on insurance held in an APRA fund, especially if they then must repurchase insurance on different terms or an individual dies.

Alternatively, the Government could extend the period for inactive accounts to a longer timeframe such as 18 months or two years. This will give greater opportunity for individuals to make contributions or rollovers to fund insurance premiums and ensure an account remains active or take action to adjust their insurance strategy (e.g. take out insurance via their SMSF or in a personal capacity).

Elections for insurance on accounts with balances less than $6,000

The SMSFA is supportive of this proposal. We believe the risks stated earlier regarding a secondary APRA-regulated fund which houses insurance for an SMSF member are considerably less due to the small account balance that needs to be managed and the fact those members should be sufficiently engaged enough to 'opt-in'.

However, we are concerned that the proposed application date and requirements for funds to assess account balances and consequently notify members that their insurance policy will be terminated potentially does not allow sufficient time to be confident that members will be notified and respond as needed.

Typically, members check their superannuation fund when their annual statement is released after the end of a financial year in late July and August. Superannuation funds have encouraged members to receive their statements and other communications online. Accordingly, many members infrequently check their superannuation fund accounts online and do not constantly monitor their fund communications. Instead, a point in time check often occurs when the annual statement is issued.

The proposed ‘stocktake’ process begins on 1 April 2019 with a 1 May 2019 deadline for notifying members that their balance is below $6000 and insurance will be terminated on 1 July 2019, leaving members less than three months to notify trustees that they wish to ‘opt-in’ to continue their insurance. Given the risks that members may not be appropriately notified of their insurance status, we believe this notification period is too short and should be expanded to allow for an end of financial statement publishing period to fall within the notification period. This ensures that the period when members are most engaged with their superannuation is utilised for notifying them of this significant shift in policy.

Accordingly, we believe the Government should extend the starting date of the legislation to 1 January 2020 to ensure that members have sufficient time to ‘opt-in’. This will allow leverage of the end of financial year period where members are likely to engage with their fund and also allow funds a longer time period to issue multiple communications.

We encourage a strong media and educational campaign to alert members their insurance may be cancelled if they take no action.

Inactive low-balance accounts and consolidation into active accounts

The SMSFA supports the reunification of superannuation balances for individuals with inactive accounts below $6,000. As stated before, many SMSF members continue to have an APRA-regulated fund open for insurance premiums. Therefore, we support the inclusion of the legislation that does not require the superannuation provider to pay an amount to the Commissioner until the insurance cover for which a member has paid for expires.

We support the mirroring of logic in the Superannuation (Government Co-contribution for Low Income Earners) Regulation 2004 to determine which superannuation fund the Commissioner is to choose to pay superannuation amounts where there is more than one ‘active’ account.

If you have any questions about our submission please do not hesitate in contacting us.

Yours sincerely,

John L Maroney

John Maroney
CEO
SMSF Association

ABOUT THE SMSF ASSOCIATION

The SMSF Association is the peak professional body representing SMSF sector which is comprised of over 1.1 million SMSF members who have $720 billion of funds under management and a diverse range of financial professionals servicing SMSFs. The SMSF Association continues to build integrity through professional and education standards for advisors and education standards for trustees. The SMSF Association consists of professional members, principally accountants, auditors, lawyers, financial planners and other professionals such as tax professionals and actuaries. Additionally, the SMSF Association represents SMSF trustee members and provides them access to independent education materials to assist them in the running of their SMSF.