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Review of Occupational Exclusions in Default Insurance offered through MySuper Products

Consultation paper

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Consultation Process

Request for feedback and comments

Interested parties are invited to comment on this consultation paper. While submissions may be lodged electronically or by post, electronic lodgement is preferred. For accessibility reasons, please submit responses sent via email in a Word or RTF format. An additional PDF version may also be submitted.

All information (including name and address details) contained in submissions will be made available to the public on the Treasury website unless you indicate that you would like all or part of your submission to remain in confidence. Automatically generated confidentiality statements in emails are not sufficient for this purpose. If you would like only part of your submission to remain confidential, please provide this information clearly marked as such in a separate attachment.

Closing date for submissions: 14 October 2021

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The principles outlined in this paper have not received Government approval and are not yet law. As a consequence, this paper is merely a guide as to how the principles might operate.

Review of Occupational Exclusions in Default Insurance offered through MySuper Products

Introduction

On 16 June 2021, the Government committed that Treasury would undertake a review into determining the appropriateness of occupational exclusions in default insurance in MySuper products. Occupational exclusions mean that insurance cover is not available (or only partial cover is available) for certain occupations that the insurer has classified as higher risk.

Many MySuper products do not have occupational exclusions for life and Total and Permanent Disability (TPD) insurance in their default insurance policies. Preliminary Treasury analysis found that nine of the top ten largest MySuper products by assets do not have occupational exclusions for default life and TPD insurance[1]. More recently, there has been a trend towards MySuper products containing no occupational exclusions.

Nevertheless, occupational exclusions have been used to alter the terms and conditions of automatic insurance cover a MySuper member may otherwise receive or restricts a member's ability to receive any insurance cover, based solely on the occupation of the individual.

Occupational exclusions affect the automatic acceptance of default cover for some new MySuper members and may also have significant consequences where a member changes occupation. The review seeks views on the two related issues when assessing the appropriateness of occupational exclusions in current industry practices:

1. Occupational exclusions that affect automatic acceptance of default cover – which can impede new MySuper members from getting default cover; and
2. Occupational exclusions that are applied when individuals change jobs – which can lead to the loss of default cover.

Consultation scope and objectives

The review is to consider whether occupational exclusions in relation to default life and TPD insurance in MySuper products are necessary or appropriate.

This review will focus on default cover in respect of life and TPD insurance which trustees are required to provide to their MySuper members. Insurance in excess of default cover, such as optional units, and income protection, will not form part of this review. These types of insurance cover have to be agreed to by members and are often underwritten or taken out after receiving advice.

The objective of this consultation is to canvass views from interested parties on the extent of the problem arising from occupational exclusions for new members and for members changing jobs and what options, if any, may be required for changes to the current regulatory framework. Stakeholder views are sought on the following options aimed at considering the necessity and appropriateness of occupational exclusions in relation to default life and TPD insurance in MySuper products:

- Option 1: No change.
- Option 2: Strengthen disclosure of occupational exclusions.

[1] Based on superannuation funds' Product Disclosure Statements and Insurance Guides accessed on 25 May 2021.

- Option 3: Members retain their insurance coverage when they change occupations.
- Option 4: Ban occupational exclusions.

Submissions are due by 14 October 2021.

Default insurance in MySuper products

The *Superannuation Industry (Supervision) Act 1993*[2] (SIS Act) requires that superannuation trustees provide their MySuper members with insurance cover in respect of life and TPD.[3] Default insurance within MySuper products must generally be provided to members on an opt-out basis.[4]

Trustees of superannuation funds are governed by a duty to act in the best financial interests of members when designing their insurance offerings, as well as to only offer insurance if the cost does not inappropriately erode the retirement income of beneficiaries.[5] Trustees are also required to regularly review the appropriateness of their insurance offering in relation to their membership pool[6] and this is particularly important when composition of their funds' membership pool changes.

Trustees must disclose eligibility criteria for the cover and include information about any applicable conditions and exclusions in the Product Disclosure Statement.

However, under the law, specifically section 68AA(3) of the SIS Act, trustees may determine 'reasonable conditions' for the provision of insurance cover for permanent incapacity benefit and death benefit. The trustee does not need to provide the insurance cover to a member if those reasonable conditions are not met.

Stakeholders have questioned whether this feature of law allows a common interpretation of 'reasonable conditions' that would be in line with community expectations for compulsory default superannuation products. The Australian Prudential Regulation Authority (APRA)'s guidance, Prudential Practice Guide SPG 250 – Insurance in Superannuation (SPG 250) reiterates the legislative framework outlined in section 68AA(4) which notes that conditions are 'reasonable if they are the same as the terms and conditions of the policy of insurance taken out to provide the benefit.'

APRA notes at paragraph 33 of SPG 250 that:

"APRA expects that an RSE licensee, when selecting an insurer, would consider the cost of insurance as one of many considerations that inform the selection process. Other important factors include, but are not limited to:

a) whether the insured benefits under consideration align with the best interests of beneficiaries more broadly;

b) the appropriateness of the terms and conditions of the insurance cover provided to any given group of beneficiaries, including takeover terms;

c) the services offered by the insurer under the agreements accompanying the insurance policy, including claims and data management, underwriting and reporting provisions; and

d) the insurer's long-term viability or sustainability."

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[2] SIS Act, s 68AA.

[3] Superannuation trustees are also permitted, but not required, to provide their MySuper members with income protection (IP) insurance.

[4] The exception being for young members and members with inactive and low balance accounts captured by the Protecting Your Super and Putting Members' Interests First reforms (see 'Related Inquiries and reforms to insurance in superannuation').

[5] SIS Act, s 52.

[6] SIS Act, s 52(7)(c).

Section 68AA(4) of the SIS Act allows trustees to determine 'reasonable conditions' and is being interpreted by some in the industry as any condition agreed in a group insurance contract is a reasonable condition. Trustees have used this discretion to determine the design and parameters of the insurance offering through their MySuper product, with the result being a wide variation in the default insurance provided to MySuper members. This includes variation in the terms and conditions, exclusions, and level of cover.

The variability of terms and exclusions leads to complexity which could make it difficult for some members to fully understand whether they will be covered by default insurance and the limitations of their insurance cover should they change occupations.

The Productivity Commission's (PC) report *Superannuation: Assessing Competitiveness and Efficiency* 2019[7] found that complexity and lack of standardisation in insurance product offerings impede member engagement and members' decisions to retain, amend or cancel their cover, thereby reducing the overall value of insurance to members.

Specifically, the PC pointed to variable eligibility definitions and exclusions as particular problems that make it difficult for members to understand what their insurance covers, which may also lead to a failure to claim entitlements. Commissioner Hayne, in the Final Report of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry (Hayne Royal Commission), also noted that "(i)nsurance contracts can often be difficult for the average consumer to navigate and understand. And subtle differences in definitions, terms and exclusions from one policy to another can make the task of comparing policies particularly challenging".[8]

Related inquiries and reforms to insurance in superannuation

While these issues are beyond the scope of this review, this section details related inquiries and reforms to insurance in superannuation. The PC's 2019 report recommended a number of areas for reform, several of which were also highlighted by the Hayne Royal Commission.

One of the PC's recommendations was for the Government to undertake an independent inquiry into insurance in superannuation within four years of the report (that is, by the end of 2022), including on the costs and benefits of insurance and whether more prescriptive regulation is required.

Several elements of the PC recommendations have already been addressed by the Government, including the *Protecting Your Super* and *Putting Members' Interests First* reforms which make insurance in superannuation opt-in for members under 25 years, members with balances under $6,000, and for inactive accounts which have not received a contribution for 16 months or more.

These changes were designed to protect superannuation savings from undue erosion by fees and insurance premiums, specifically in relation to accounts which are most at risk of erosion (low balance and inactive accounts), and in relation to those cohorts of members who are least likely to receive value for money for insurance they may not need, may not be able to claim on, and may not even know they are paying for (members under the age of 25). Importantly, trustees can elect to opt-out of these reforms in relation to members under 25 years old or with low balances who are employed in the top riskiest quintile of dangerous occupations, or are employed as emergency services workers.

The Hayne Royal Commission recommended that the Government consult with industry on the practicability and likely pricing impacts of standardising key definitions, terms and exclusions for default MySuper group life policies (Recommendation 4.13).

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[7] Productivity Commission, *Superannuation: Assessing Efficiency and Competitiveness*, 2018.
[8] Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry, Final Report, p 322.

Treasury implemented this recommendation in 2019, with over 20 submissions received through the consultation process. Overall, while stakeholders were supportive of some degree of standardisation of terms to improve consumer understanding and comparability, it was strongly recommended that trustees retain the ability to design insurance offerings to the needs of members.

Occupational exclusions in default insurance in MySuper products

Occupational exclusions apply where an insurer identifies certain occupations that are associated with higher risks and hence exclude members in those occupations from being eligible for insurance cover or only provide partial cover.

In some circumstances, for example where the fund is a corporate scheme for a particular industry, this approach has historically made sense, but as superannuation funds' members grow and serve a more diverse membership, occupational exclusions within a MySuper offering may potentially deny new members from accessing insurance and affect existing members' ability to keep insurance when changing occupations. These issues faced by members raise questions on the appropriateness of occupational exclusions, given the changed environment that the superannuation industry now operates in.

Exclusions can take various forms. For example, some funds exclude certain occupations from automatic default life and TPD insurance cover; apply different definitions used to assess a claim depending on the individual's occupational circumstances at claim time; or alter the sum insured.

As a result, notwithstanding disclosures available, members may assume their insurance cover does not contain any exclusions relating to their occupation, only to encounter difficulties claiming following an insurable event and not receiving the insurance payout that they would have received if they were in a MySuper product that did not contain any occupational exclusions. This is a problem that is already present in the superannuation system and is consistent with the generally low levels of engagement from members with their superannuation and associated insurance cover.

Disclosure of members' occupation is critical for trustees and for insurers in pricing risk. Trustees are often reliant on employers to disclose whether a member is in a high-risk occupation. However, trustees may not have accurate, or indeed any, information regarding the members' occupation. If insurers are not aware of how many high-risk members they are covering then they are likely to take a conservative view and overprice the risk. This will impact all members if this overpricing is passed on to all occupation groups. This might result in trustees deducting repayment of higher premiums from the sum insured or cancelling the default cover and refunding the premiums when members in high-risk occupations make a claim.

Scenarios on effect of occupational exclusions

The following examples are scenarios relating to occupational exclusions which may impede MySuper members from receiving the benefits of default insurance that they may need.

These scenarios are based on some existing industry insurance products.

Scenario 1: Occupational exclusions that affect automatic acceptance of default cover

Chiara works full time as a jockey. She was defaulted into a MySuper product when she started her first job, and upon receiving her member information pack, she learned that she had been given default life and TPD insurance cover.

While working Chiara suffers a serious fall from a horse and is severely injured. She may not be able to work again. When she applies to her fund and insurer to make a claim, she is told that they were unaware of her occupation, and the high-risk nature of it. 'Jockey' is listed as an occupation that is excluded from cover on the basis of being 'uninsurable'. As a result, the insurer rejects the claim, and cancels Chiara's insurance cover.

Scenario 2: Occupational exclusions that are applied when individuals change jobs

2A. Application of occupational exclusions where a member informs fund of hazardous occupation

Amelia is employed in a non-hazardous occupation as a dental receptionist. When she started her job, she was defaulted into her employer's default fund, Dental Super Fund, and therefore automatically received default insurance cover.

Amelia subsequently starts working as scuba diver. She informs her fund of her new occupation and is informed that scuba diving is classed as a hazardous occupation which the fund's default insurance does not cover. Amelia loses her default insurance cover (or is given the option to only retain partial cover). This was due to the fact that Dental Super's default insurance policy contained an occupational exclusion for scuba divers.

2B. Assessment under more restrictive eligibility criteria as a result of hazardous occupation

Jonathan is employed in a non-hazardous occupation as a retail assistant in a large department store. He is eligible to receive default insurance at the time of joining his super fund as a MySuper member.

Jonathan subsequently leaves his job as a retail assistant and starts working full time in a mine. Jonathan retains his existing super fund and the default insurance cover after he started working at the mine as his fund does not have occupational exclusions.

However, a few months later Jonathan is involved in an accident at the mine and suffers serious physical injuries. Jonathan is told he is able to make a claim under his default insurance, however he will be assessed under a more restrictive TPD definition, compared to the eligibility definition that would be applied if he had suffered an insurable event in his previous, non-hazardous occupation.

Potential options

Stakeholder views are sought on the following options aimed at considering the necessity and appropriateness of occupational exclusions in relation to default insurance in MySuper products. In particular, these options are aimed at addressing the following concerns about occupational exclusions: the disclosure of occupational exclusions; members losing default insurance after they move into a higher risk occupation; and members not being able to get automatic acceptance of default cover.

These options require careful consideration and identification of relevant scenarios and their consequences.

Option 1: No change.

The review is seeking views on the extent to which the current regulatory framework has the potential to result in some members having inappropriate life and TPD insurance through their MySuper product and whether Government intervention is required or not as the industry continues its trend towards removing occupational exclusions.

Option 2: Strengthen disclosure of occupational exclusions.

The adequacy of information to inform individual choice of superannuation and associated insurance will also be considered along with whether further steps could be taken to strengthen disclosure to members in an accessible and easy to understand way. For example, this could include a requirement to disclose occupational exclusions within a brief, standard template that better supports comparisons across products.

This option may particularly support those workers that actively engage in comparing and choosing their superannuation. Consideration could be given to coupling Option 2 with Option 3.

Option 3: Members retain their insurance coverage when they change occupations.

This option addresses the issue of members losing default insurance after changing occupations (Scenario 2).

Under this option, members do not lose their default insurance when they change occupations, regardless of any occupational exclusions that apply to their new occupation in the insurance policy they hold. That is, where a member holds insurance for their current occupation, when they change occupations, they cannot subsequently be subject to occupational exclusions.

Views are sought on the merits and feasibility of this option and on alternative mechanisms to ensure members have appropriate insurance coverage when they change occupations. Consideration could be given to the costs and benefits of Option 3 compared with Option 4.

Option 4: Ban occupational exclusions.

This option addresses both members not being able to get automatic acceptance of default cover (Scenario 1) and the loss of default cover after changing occupations (Scenario 2).

The necessity and appropriateness for occupational exclusions in default life and TPD insurance offerings within MySuper products will be considered. Consideration will also be given to other occupation-related clauses in group insurance policies in a broad sense where an insurer could deny a member's insurance claim due to the nature of their employment.

Views are sought on the merits and feasibility of this option, including implementation considerations and available trustee responses to ensure that members are not faced with other forms of eligibility restrictions based on specific work activities or occupation.

Discussion questions

1. What is the prevalence of occupational exclusions on default life and TPD insurance offerings within MySuper products?

    1.1. How widespread are occupational exclusions affecting automatic acceptance when a member first becomes a MySuper member?

    1.2. How widespread are occupational exclusions that affect existing default cover when a member changes occupation?

2. Do trustees have access to data to understand their members' occupations and tailor the cover accordingly? What should trustees and insurers do to better capture and assess the changing occupations of their members?

3. Is there scope to strengthen standardised disclosures or improve communication to members to assist them to understand their insurance cover, particularly when occupation exclusions apply? Would Option 2 adequately address the problem?

4. Are there benefits of occupational exclusions that would justify some funds maintaining them? What are the costs of occupational exclusions and should funds be required to remove them?

5. What would be the implications on pricing, benefit design/default levels of cover and claims rates under Options 3 and 4? How would these implications be addressed? How do the costs and benefits compare between Options 3 and 4?

6. If Option 4 was adopted, what responses should be made available to trustees and insurers and why? What would be the appropriate implementation mechanism, necessary transition periods and consequences for non-compliance (if applicable)?