



Superannuation Stage 3: Assessing Competitiveness and Efficiency

MLC Life Insurance submission to Productivity Commission
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MLC Life Insurance welcomes the opportunity to provide a submission to Stage 3 of the Productivity Commission's inquiry into the competitiveness and efficiency of Australia's superannuation system. In doing so we note the Terms of Reference require the Commission to consider the appropriateness of the insurance arrangements inside superannuation. We also note the numerous insurance in superannuation matters raised in the issues paper *Superannuation: Assessing Competitiveness and Efficiency*.

As both a market participant and an advocate of the many benefits of life insurance, MLC Life Insurance strongly supports the maintenance of "opt out" life insurance in superannuation arrangements and the numerous benefits it brings. Key amongst these are:

- For many Australians, the life insurance, disability and income protection insurance they purchase through their superannuation is the only insurance they have. If life insurance in superannuation did not exist, underinsurance would be a much bigger issue and more individuals and families would be financially challenged when dealing with injury, sickness or death. A secondary consequence would be an enlarged burden on government as it assisted individuals in dealing with these challenges.
- Life insurance in superannuation is generally provided on an auto-acceptance basis with no or limited eligibility requirements and no or limited underwriting. This helps make insurance cover more widely available, including to those who would not otherwise be able to obtain insurance due to their health history, lifestyle, occupation or employment status.
- The provision of automatic "opt-out" cover also means that life insurance in superannuation takes all risks, good and bad. If cover were shifted to an "opt-in" basis, the risk profile of the insured population would be likely to change and this could lead to negative impacts on all insurance in superannuation members, including a decrease in affordability.

MLC Life Insurance strongly believes life insurance in superannuation is consistent with the superannuation sole purpose test¹ because the purpose of insurance products is to assist with:

- a reduced ability to earn a consistent income prior to retirement (either via income protection cover or lump sum total and permanent disability cover)
- the financial impact of premature death, by enabling debts to be settled so as to not leave a burden for beneficiaries, or to provide beneficiaries with a sum of money which represents the financial support they may have looked to from the deceased, had they continued to live.

MLC Life Insurance notes the 2010 Cooper Review into the governance, efficiency, structure and operation of Australia's superannuation system supported this view, finding that "insurance was a valuable aspect of superannuation as it provides benefits to members (and their dependants) when members are no longer able to work due to death or total and permanent disablement (TPD) before normal retirement age".

The current opt-out model of superannuation in insurance is based on sound principles. In 2013 the StrongerSuper reforms set out a requirement for default *MySuper* superannuation products to contain a minimum default level of life insurance and specified what those minimums are to be. This decision was based upon the rationale that superannuation members opting for the *MySuper* product option were less likely to have considered their insurance needs. Therefore policy makers felt it necessary for a default level of cover to be provided to those members, albeit with the opportunity to choose to opt out.

Notwithstanding the strong arguments in support of the opt-out model of life insurance in superannuation, MLC Life Insurance recognises there are numerous opportunities to improve the system. We are a strong advocate of extending many of the beneficial consumer protections found in the *Life Insurance Code of Practice* to insurance in

¹ The sole purpose test ensures a superannuation fund is maintained for the purpose of providing benefits to its members upon their retirement (or attainment of a certain age), or for beneficiaries if a member dies.

superannuation, and support the efforts of the *Insurance in Superannuation Working Group* to achieve this goal. We also support moves to improve aspects of insurance in superannuation, including:

- Making opting out of insurance easier for members. Our new *LifeView* digital platform launched in July 2017 does this by offering a means to opt out online².
- Ensuring benefit design is age appropriate. The role of trustees and their understanding of their membership risk profile is paramount to this objective.
- Minimising the erosion of superannuation balances, especially for younger and lower income members.
- Reducing the incidence of consumers being charged multiple insurance premiums, by addressing the underlying issue of multiple accounts.
- Improvements in claims handling through clearer timeframes, service standards and communications.
- Improving communications, education and awareness of insurance amongst superannuation fund members.

About MLC Life Insurance

MLC Life Insurance, which traces its origins back to 1886, has 1.4 million customers and is still fulfilling its original goal: “to bring the security and protection of life assurance within the reach of every man, woman and child”.

On 3 October 2016 National Australia Bank Limited (NAB) completed its sale of 80% of its interest in MLC Limited (MLC Life Insurance) to the Nippon Life Insurance Company (Nippon Life). This has led to the creation of a specialised life insurance business, MLC Life Insurance, where Nippon Life has a majority 80% holding, while NAB retains 20%.

With a market share of approximately 11%, we are Australia’s third largest life insurer. Traditionally our focus has been on the retail market segment where policies are sold via financial advisers, but our involvement in the insurance in superannuation market is growing. Our group insurance inforce premium is approaching \$600m, equal to a market share of approximately 8%³. We are seeking to continue to our presence in this market, particularly in the important industry superannuation fund segment, to which we are bringing new innovation and competition.

Regardless of channel, our products play an important role in protecting our customers, their families and businesses against the adverse financial impacts of premature death, illness, injury or disability. In the financial year to 30 September 2016, we paid over \$900m in claims for our customers and their families, in doing so reducing or removing the need for people to rely on government and taxpayer support to manage their financial needs and responsibilities. 1,701 customers were supported through occupational rehabilitation and recovery services during the same period, helping them regain ability and normalcy in their lives.

With the strong backing of Nippon Life, MLC Life Insurance is now poised to deliver even better value for its customers. This strategic partnership is enabling us to invest significant capital (in the order of \$400 million) to simplify and improve the customer, member, trustee, adviser, banker and employee experience with the aim of ensuring our insurance products are easy, simple to understand and administer. Digital channels and data analytics form a key part of our strategy. We are investing to simplify our back-office systems, including sales, servicing, underwriting and claims, to make it easier and faster for our stakeholders.

In making this submission MLC Life Insurance has contained its responses to matters relating to insurance in superannuation only, via selected questions from the *Superannuation: Assessing Competitiveness and Efficiency* issues paper. These questions and our responses are set out below.

² *Lifeview* also includes the ability to provide a notice to members of the potential impacts of opting out. This is important as members may unwittingly ‘opt out’ not realising that if they wish to later rejoin they will almost certainly need to provide evidence of good health in order to gain cover.

³ NMG Consulting, *Group Channel Risk Distribution Monitor*, June 2017

Page 13**What are the material policy or regulatory impediments to the competitiveness and efficiency of the superannuation system?*****Multiple accounts***

MLC Life Insurance considers one of the key impediments to the efficiency of the superannuation system is the creation of multiple accounts, which results in multiple fees being charged, including multiple insurance premiums. While making it easier for superannuation members to opt out of insurance is one way to start to address this problem, we consider a better way to address this issue is by preventing the creation of unwanted accounts, or improving the account consolidation processes.

Directionally we support the proposition aired in the *Superannuation: Alternative Default Models* draft report produced in Stage 2 of this inquiry to introduce mechanisms to limit the creation of new superannuation accounts. However we have concerns the proposed mechanism may result in large numbers of people maintaining the account created in their first occupation and that this may not be appropriate to their circumstances in later life. It would likely also lead to a proliferation in membership taxonomies within individual superannuation funds, complicating the trustee's ability meet their legal responsibilities.

An alternative option may to permit new employers to create a new account, but to require the trustees administering the new account to automatically consolidate previous accounts into the new account, unless the member directs this not to occur. Allowing the member to make this choice is important as, for a range of reasons, some members purposefully hold more than one superannuation account. One reason some superannuation members maintain multiple accounts is to retain access to the insurance arrangements that exists on the account. For this reason we would support the owners of newly created accounts also being given the option of transferring in insurance arrangements from other accounts.

Collection and payment of Superannuation Guarantee contributions

To facilitate the above and reduce incidences of unpaid Superannuation contributions, MLC Life Insurance supports the Australian Taxation Office (ATO) taking on the centralised clearing house role touched upon in *Superannuation: Alternative Default Models*. The ATO already captures employee wage information and receives tax remittances from employers; it should be relatively easy for employers to also pay Superannuation contributions to the ATO and for it to disburse this to Superannuation funds.

**Page 15
(Table 2)****Case study and other evidence demonstrating the ease and extent of members opting out of insurance, amending cover or making claims.**

MLC Life Insurance strongly supports the maintenance of opt-out life insurance in superannuation arrangements. For many Australians, life insurance through superannuation is the only life insurance they have and without it more individuals and families would be financial challenged when dealing with injury, sickness or death. Nonetheless we recognise the opt-out system can be improved, especially by making it easier for superannuation members to understand their insurance and to manage their account.

Investment in member and trustee facing systems is central to the goal of making insurance easier to understand and manage. In August 2017 we launched a new digital platform called *LifeView*, a secure online portal accessible to the members, administrators and trustees of superannuation funds affiliated with MLC Life Insurance. The *LifeView* platform will provide members with an alternative to paper based communications with their superannuation fund or MLC Life Insurance when managing the most common life insurance needs such as opting out of insurance, amending their cover and lodging and tracking the progress of claims.

In respect of managing the needs related to ongoing membership, we expect *LifeView* to benefit members in a number of ways:

- Members considering changing their cover will have access to tools including a needs analysis tool and a premium calculator.
- Having decided to change their cover members can do so via *LifeView*, including increasing or decreasing cover, changing their occupation category, changing a waiting period or changing a benefit period.
- Where the change requires underwriting, *LifeView* will automatically ask health and lifestyle questions. In 50-60% of cases a decision is able to be made on the spot, meaning the majority of applications can be completed in minutes.
- *LifeView* removes the need for a number of previously manual claims processes, shortening claim handling time and enabling claim progress to be tracked online.

Because it makes engaging with their life insurance easier, we expect *LifeView* to improve levels of life insurance understanding amongst superannuation members due to the many tools and resources incorporated into the system.

Communicating the implications of opting out of life insurance

In respect of superannuation members opting-out of their life insurance, any policy changes intended to make it easier for superannuation members to opt-out should require members to be fully informed of the implications of doing so. In particular members must be informed they will typically need to provide personal health, occupational and lifestyle information and have that information assessed before they will be able to obtain cover again⁴. We recommend that as part of the opt-out process members be clearly informed on:

- the insurers reinstatement policy
- the circumstances (if any) in which an opt out decision can be reversed
- the consequences of opting out for future insurance via their superannuation fund, including that members who wish to take up insurance again at a future date will generally not be automatically accepted or may face restrictions on their cover
- the sort of personal and health information that the member will be required to provide if they later seek to add life insurance to their superannuation membership.

Page 15 (Table 2)	Case study and other evidence demonstrating funds' use of member information to provide default insurance cover
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For much of the history of the Australian superannuation system a large proportion of superannuation members were in their default industry, public sector or employer fund. The specific nature of these funds meant they had a specialised knowledge of the risks associated with the occupations within it. This allowed superannuation funds, with the support of their life insurer, to rely on three key pieces of information when designing life insurance benefits:

- the member's gender
- the member's date of birth
- the member's occupation, or if this information was not available, their industry as a proxy for their occupation.

⁴ Depending on the superfund, the applying member may only be granted cover if they meet an acceptable level of health, or may only be covered on a restricted basis under a pre-existing condition clause.

The introduction of Super Choice in 2005 precipitated an expansion in the range of occupations within the insured populations of industry funds and the slow decline of employer funds, a trend that has accelerated as funds have merged. As a result, the ability for funds to rely on these three listed data points has deteriorated.

Superannuation funds are responding to this challenge in different ways. Some funds are now introducing occupational ratings to ensure competitive pricing by occupation. Generally, however, incoming members are defaulted to the most expensive occupational rating and they need to apply to the fund to change their occupational status so as to obtain improved premiums. In addition, some funds have reduced or capped the premium burden on younger members by reducing death and total and permanent disability benefits.

A more sophisticated approach is to move to a more “needs based” design, whereby member’s needs are defined based upon a combination of age and life stage. The case study below sets out an example of how this has been jointly implemented by MLC Life Insurance and a partner superannuation fund, based on the concept of “life-stage”.

Case study: a life-stage design approach to insurance in superannuation

In this example the goal of the Trustees was to provide a sophisticated Trustee Default cover, comprising opt out TPD and death cover, for use when neither a member nor their employer make an active choice of cover. Core to this goal was the understanding that a superannuation fund member’s insurance needs change in response to certain relatively predictable life events, such as taking on a mortgage or changing levels of dependency. These events tend to cluster around certain ages, which permitted MLC Life Insurance and the Trustees to design a life-stage approach that automatically varies the level of Trustee Default cover and associated premiums so as to provide financial protection during the years when it is most needed.

Basic attributes of the Trustee Default cover

When designing or redesigning the Trustee Default cover, the Trustee considers the following attributes of the member base of the superannuation fund:

- average member account value
- age profile of the fund
- average Superannuation Guarantee contribution
- average insurance premium
- percentage of members who opt out of cover
- terms of cover of the default insurance options
- change in primary household debt levels
- changes in the future costs of dependants
- outlier member impacts.

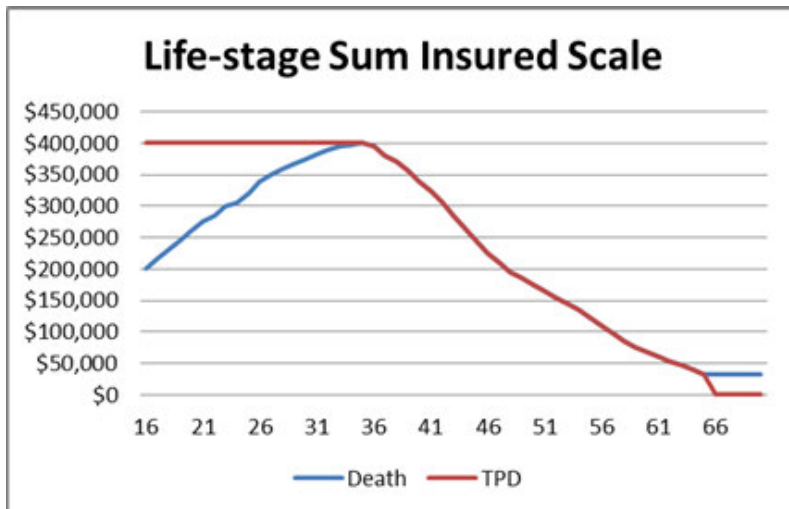
Adding in life-stage attributes

Added to the basic attributes listed above are life-stage attributes including:

- mortgage lending values
- Australian Bureau of Statistics data on the number and cost of dependants, based on a given age range
- data on years of dependency
- the present value of the cost of a dependant.

Design outcome

Based on the attributes above, the current Trustee Default cover developed to cover the basic insurance needs of Members of the fund is displayed in the chart below:



Where to next?

Consumers would benefit if superannuation funds could more accurately optimise cover so that it was able to be efficiently mass-customised. A mass customisation approach could work since it can be achieved without trying to force greater levels of contact and collaboration between superannuation funds and their members (which to date large numbers of superannuation members appear reluctant to do), but doing so is dependent on collecting more information at the individual member level, in particular personal and financial information. Funds could then work with their insurer to undertake econometric and statistical analysis to build a benefit and premium design appropriate to specific cohorts of members.

Page 26 (Table 3)	Main additional evidence needs and sources	
Insurance		
Impact of insurance on retirement balances	<p>Given insurance in superannuation premiums are deducted from a superannuation member’s account, it is manifestly self-evident that the balance of an insured person’s superannuation account is lower at retirement than it would be than if no premium had been deducted.</p> <p>The challenge that faces superannuation trustees and their insurance partners is to ensure the impact on member’s balances is not inappropriate or excessive⁵. This is achieved when the superannuation fund provides a product that is appropriate to its members’ circumstances and represents good value.</p> <p>The ability of Superannuation funds to achieve this would be enhanced if they collected more data about their members. While funds can use Superannuation Guarantee contributions to infer a members salary level, if they had more information about the members dependents or financial status it could use the information to inform benefit design. Superannuation funds</p>	

⁵ This requirement is also expressed in legislation. Section 52 7 (c) of the *Superannuation Industry (Supervision) Act 1993* (Cth) requires fund trustees 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”.

	<p>should also actively monitor for the receipt of Superannuation Guarantee contributions so they know if a member is in or out of employment. This would allow funds to switch on or off components of the insurance, such as income protection products where no benefit is payable if the member is out of employment.</p>
Insurance cover by age band and market segment, existence and consolidation of duplicate policies, take-up in choice products	MLC Life Insurance supports superannuation funds actively managing duplicate accounts within their own fund, and to promote account consolidation to their membership base.
Comparison of premiums inside and outside of superannuation and historical ratio of claims to premium revenue	<p>A straight side by side comparison of retail and superannuation product premiums would be misleading. To properly compare the premiums of the two products requires controlling for the very different features present in the two markets. Examples of factors to take into account include:</p> <ul style="list-style-type: none"> • Retail insurance is an underwritten, risk rated product, compared to default insurance in superannuation products being auto-acceptance, community rated products. • Different product mix in each channel. • Difficulty of obtaining consistent data, even within a particular channel. This impacts on the ability to build a comprehensive picture of key factors, for example claims experience⁶. • Different costs of customer acquisition in each channel. • Specific features of either channel that have no equivalent in the other, such as trailing commissions in retail life insurance or profit-sharing arrangements in insurance in superannuation.
Effect of policy settings on social security costs to Government	<p>Apart from the direct benefit to the state and federal government through avoided disability, health and social security costs, insurance in superannuation also creates economic benefits by way of its efforts to support injured or unwell people back into the workforce.</p> <p>There are multiple beneficiaries of this support:</p> <ul style="list-style-type: none"> • The supported person benefits by being returned to a healthy and productive lifestyle) • Insurers benefit because returning claimants to work results in decreased overall claims costs. • All customers benefit when decreased claims costs translate into more affordable premiums. • Employers benefit from regaining the productive labour of their employees. <p>There is an important wider benefit as well. There is substantial evidence demonstrating the link between disablement and lower rates of labour force participation⁷. Therefore, in seeking to obtain the commercial benefits available from supporting injured or unwell people back into the workforce,</p>

⁶ We note that work currently being undertaken by APRA to collect claims outcomes data could ultimately be useful here.

⁷ Mavromaras, K; Oguzoglu, U; Black, D and Wilkins, R. *Disability and Employment in the Australian Labour Market*, Melbourne Institute of Applied Economic and Social Research, 2007

	<p>insurers also create spill-over benefits at the macro-economic level by way of supporting labour force participation and productivity.</p> <p>This is particularly the case given evidence demonstrates that the longer a customer is away from their work and usual routines of life, the more likely they are to become permanently dislocated, including being unable to work. For example:</p> <ul style="list-style-type: none"> • If a person is off work for 20 days the chance of ever getting back to work is 70%. • If a person is off work for 45 days the chance of ever getting back to work is 50%. • If a person is off work for 70 days the chance of ever getting back to work is 35%⁸. <p>If less working people had income protection insurance through their superannuation, not only might they be more likely to seek government social security benefits, they would be more likely to be out of the workforce for a long term period and perhaps permanently.</p>
Ease and extent of members opting out of insurance, amending cover or making claims	Please see response on pages 4-5 above.
Funds' use of member information to provide default insurance cover	Please see response on page 5-7 above.

⁸ Australasian Faculty of Occupational and Environmental Medicine, *Realising the Health Benefits of Work*, 2011, p. 12, <https://www.racp.edu.au/advocacy/division-faculty-and-chapter-priorities/faculty-of-occupational-environmental-medicine/health-benefits-of-good-work>

Commentary on *The Commission's assessment framework*

The following tables contain general commentary on selected insurance related sections of Attachment B of *Superannuation: Assessing Competitiveness and Efficiency*.

Page 35	Objective 4: The superannuation system provides value for money insurance cover without unduly eroding member balances	
E11. Do funds offer value for money insurance products to members?		
Duplicate insurance policies (output)	MLC Life Insurance recommends the issue of duplicate insurance policies is best dealt with by solving for the larger issue of duplicate superannuation accounts. For more information please see response on page 4 above.	
Rates of insurance take-up in choice products relative to default products (output)	Not addressed.	
Member superannuation and insurance literacy (input)	MLC Life Insurance supports initiatives for financial literacy, including insurance literacy, to be improved amongst Australian's of all ages. Improved levels of financial literacy would equip finance system users with an enhanced ability to manage their own financial interests and so should lead to improved consumer outcomes. Given this we welcome the Australian Government's recent announcement of new funding to support the states and territory governments to deliver the ASIC MoneySmart Teaching program.	
Ease of members opting out of insurance, amending cover or making claims (input)	Please see response on page 4-5 above.	
Number of members changing or opting out of default insurance cover (input)	<p>MLC Life Insurance is pleased to provide data relating to a large, multi-employer default superannuation product we insure.</p> <p>For that product, out of 613,835 total members:</p> <ul style="list-style-type: none"> • 440,476 members (72%) have default insurance. • 24,863 members (4%) have opted to increase their insurance. • 148,496 members (24%) have either cancelled their insurance or their insurance has lapsed due to low balance. 	
Funds' use of member information to inform product design and pricing (input)	Please see response on page 5-7 above.	
Comparability of insurance product information disclosed by funds (input)	Not addressed.	
Average insurance cover by age band and market segment (output)	Not addressed.	
Proportion of complaints to the Superannuation Complaints Tribunal which are successful (output)	Not addressed.	
Number of members that	Not addressed.	

nominate beneficiaries (input)	
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Page 35	Objective 4: The superannuation system provides value for money insurance cover without unduly eroding member balances
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E12. Are the costs of insurance being minimised for the level and quality of cover?
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Insurance premiums inside compared to outside superannuation for like policies (output)	The risk premium cost is the same for in super and outside of super policies if their terms e.g. automatic acceptance are the same. Likewise the insurers statutory responsibilities to insured members is the same under either construct.
Insurance expenses (incurred by funds) (input)	Superannuation fund insurance expenses can be variable depending upon the benefit design, complexity and service standards agreed with their insurer. Overall insurance in superannuation is very efficient, as demonstrated by the long run industry average loss ratio of approximately 81%.
Insurance premiums paid by members as a percentage of Superannuation Guarantee contributions made by insured members (output)	Not addressed.
Ratio of claims to premium revenue (loss ratio) within superannuation over 5 and 10 year periods (output)	Not addressed.
Fee and premium differences from outsourcing insurance services to related versus unrelated parties (output)	Not addressed.
Proportion of APRA-regulated institutional funds switching their insurance provider (input)	Not addressed.
Trailing adviser commissions embedded in choice products and insurance (output)	Not addressed.