SUBMISSION WITH RESPECT TO THE FINANCIAL SYSTEM INQUIRY INTERIM REPORT

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This is a short submission which deals with a few issues raised in the Financial System Inquiry (FSI) Interim Report.

1. General

We generally support the thrust of the Interim Report with respect to consumer needs such as the availability of information and documentation in an accessible form, financial services and products being fit for purpose and access to justice effective dispute resolution.

2. Superannuation Post Retirement Products

We agree that the superannuation policy area in most need of attention is the post retirement phase.

The Stronger Super legislative package that followed the Cooper Review in 2010 was a substantial overhaul of the superannuation system in Australia applicable to the accumulation phase.

However, it did not purport to deal with the post retirement phase, which was acknowledged at the time as the next big policy review area in superannuation.

As the baby boomers transition to retirement with substantial and growing superannuation accounts, the development of post retirement products and consumer protection is essential and urgent.

Whilst the development of a default post retirement product similar to MySuper would be problematic, consideration could be given to the development of standard income stream products into which part of a retirement lump sum could be placed. Such product should require authorisation by the Australian Prudential Regulation Authority.

However, care must be taken to ensure that such products are not miss-sold and fees gauged.

3. Superannuation Fees

The level of fees in superannuation requires constant monitoring because of the compound effect higher fees have on the size of retirement benefits.

The Interim Report rightly raised concerns about the size of fees in the compulsory superannuation environment in Australia and indicates that action may need to be taken to encourage fee-based competition.

Whilst we agree that there needs to be vigilance as to the level of fees in superannuation, we believe that the initiatives arising out of the Stronger Super reforms, specifically MySuper and

Superstream, need to be given the opportunity to work before any further significant structural amendments are considered.

MySuper was designed to reduce fees and charges for the largely disengaged majority of Australian workers and Superstream was designed to reduce the back office costs associated with the transfer of superannuation contributions, rollovers and payments.

MySuper commenced from 1 January 2014 for most new employees, with a transition period for some existing employees until July 2017. The Superstream implementation date has been put back to 1 July 2015.

It is our view that the policy setting behind both amendments arising out of the Cooper Review was sound and both are likely to have an impact on superannuation fees and costs. However, the extent to which fees will be driven down will not be assessible for at least two to three years and it would not be appropriate to consider further significant structural reforms based on a premise that fees are too high due to a lack of competition without giving these recent structural reforms the opportunity to work.

This does not mean that other measures should not be considered, where appropriate. But further major structural changes premised on a finding that superannuation fees are too high should await a review of the impact of such fundamental structural changes as MySuper and Superstream.

An added reason for a cautious approach to legislative reform is the impact of reforms on consumer confidence in the superannuation system, as well as the legal and compliance costs associated with same. The Interim Report correctly identified reform fatigue and uncertainty as affecting stability and trust in the superannuation system.

4. Underinsurance – General Insurance

The Interim Report made mention of underinsurance in both general insurance and life insurance in Australia.

General insurance products such as home and contents, motor vehicle and travel insurance policies have periodically received public attention as to the level of underinsurance. This was no better illustrated than in the transition in the problems with home and contents insurance from the availability of flood insurance cover to the affordability of home and contents policies generally.

Insurers traditionally imposed flood exclusions on home and contents insurance policies which became notorious after a number of major flood events in the 1990's and 2000's. Insurers did respond over time, particularly after the Brisbane flood in 2010, with most progressively dropping flood exclusion clauses.

However, in doing so, premiums rose, particularly for those deemed to be in "at risk" flood prone areas. This resulted in a shift to an affordability problem with many consumers opting out of insurance cover altogether.

The most serious affordability problem has occurred in Far North Queensland with home and contents insurance premiums up to 5 to 10 times higher than in other parts of the country. A number of reviews and studies have looked at the affordability problem. The writer was involved in perhaps the most contemporary review, The National Disaster Insurance Review, which recommended the establishment of a national agency to coordinate flood risk management and operate a system of premium discounts and a flood reinsurance facility, underwritten by the Commonwealth.

The NDIR made similar recommendations in relation to cyclone risk cover – although with a recommendation for a further review as to whether affordability discounts could be offered.

To date, the key recommendations of the NDIR have not been implemented and the matter could be looked at by the FSI as a means of addressing the increasing affordability problem.

5. Underinsurance – Life Insurance

The Interim Report also briefly mentioned underinsurance in life insurance.

Life insurance covers death, total and permanent disability (TPD), income protection, terminal illness and trauma insurance. All may be purchased on an individual retail basis or on a wholesale group insurance basis through, for example, employer-sponsored policies or employment superannuation. The only exception is that trauma insurance cannot be offered under group insurance through superannuation.

The symmetry between superannuation and insurance is that insurance "tops up" the retirement incomes of Australians whose working lives are cut short because of disability or death to enable them to have sufficient monies to live off in retirement. This is an important hedge against increasing reliance on Centrelink benefits, in particular the Disability Support Pension.

Although the number of Australians with life insurance has increased, primarily due to the availability of low cost Automatic Acceptance Limit wholesale insurance provided through employment superannuation, the average amount of life insurance cover is still low.

The advent of Choice of Fund legislation 2005 led to increased competition between superannuation funds, with insurance offerings being a key point of differentiation. Consequently, life insurance cover has risen significantly but it is still at suboptimal levels.

One means by which Australians have been able to enhance their life insurance has been through the adoption by many employment superannuation funds of continuing account-based insurance cover with the result that many workers with multiple superannuation accounts have multiple insurance policies which can be claimed upon.

However amendments to the Lost Superannuation legislation in 2013 increased thresholds below which inactive accounts must be paid to the Australian Taxation Office. This has meant that many inactive superannuation accounts with active insurance have been swept up and transferred to the ATO, with the loss of valuable life insurance cover (the ATO does not continue insurance cover for monies transferred to it).

The consolidation of multiple inactive superannuation accounts is laudable policy in that it reduces unnecessary multiplication of administration fees. However the unintended loss of potentially millions of insurance policies has exacerbated the underinsurance problem in

Australia, which in turn puts greater pressure on Centrelink, particularly through the Disability Support Pension.

To avoid this unintended outcome, inactive superannuation accounts with insurance cover should be exempt from auto consolidation or they should only be consolidated on an opt-in basis.

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