7 March 2014

Australian Prudential Regulation Authority
400 George Street
SYDNEY NSW 2000

Email: Insurance.Policy@apra.gov.au

Dear Sir/Madam,

Re: Draft Prudential Practice Guide LPG 270 Group Insurance Arrangements

The Australian Institute of Superannuation Trustees (AIST) is an independent, not-for-profit professional body whose mission is to protect the interests of Australia's $600 billion not-for-profit superannuation sector. AIST's members are the trustee directors and staff of industry, corporate and public-sector superannuation funds, who manage the superannuation accounts of two-thirds of the Australian workforce.

AIST welcomes the opportunity to comment on draft prudential practice guide *LPG 270: Group Insurance Arrangements* (LPG 270, "the Guide", "the Draft Guide", "the PPG"), which is designed to outline prudential practices in relation to group insurance. Whilst we understand that the intended audience of LPG 270 is intended to be life insurers, AIST is mindful that the Draft Guide should be consistent with the prudential requirements of registrable superannuation entity (RSE) licensees.

Our feedback on the Draft Guide should be viewed with this in mind.

Impact of *Prudential Standard SPS 250 Insurance in Superannuation*

AIST welcomes the note on page 3 that outlines the context for LPG 270. Whilst we understand that APRA could have taken a "end-user-agnostic" position with regards to the Draft Guide, we agree with APRA's implied position that the larger proportion of customers who purchase group insurance are RSE licensees. Accordingly, we welcome this as a focus of the document.

General comments

AIST welcomes regulatory guidance in all forms. We believe that any kind of guidance forms valuable assistance to parties affected by regulation, and support the efforts of regulators in providing this.

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We take this opportunity to recommend that, wherever possible, recommendations in this document should be crafted so that they dovetail neatly with the requirements in SPS 250. In addition, however, we also recommend that wherever possible, compatibility be put in place with recommendations contained in prudential practice guidance.

Risk management framework

AIST welcomes the list of risks that should be identified in the risk management framework, where these are material. We believe that the listing of these points will provide a great assistance to RSE licensees in assessing the impact of what is a decision to undertake a material outsourcing arrangement. We support efforts to maintain uniformity from the risk management framework provided from an insurer to an RSE licensee all the way through to assessment of how this affects the licensee's risk management framework and declarations associated with this.

We believe that paragraph 4 could benefit also from a statement that discusses the need for any group insurance arrangements to assist trustees in meeting their obligations under *Prudential Standard SPS 231 Outsourcing*. Whilst this context may not be a requirement for insurers, we point out that part of the purpose of APRA's prudential practice guides is to provide guidance on areas of "sound practice" as explained on page 3. We believe customer assistance in anticipating client needs from insurers to their clients, or effective product design may be two examples of these areas.

Insurance tenders

We believe that paragraph 6 covers an excellent set of issues to be addressed when insurers respond to tenders.

However, an issue that we believe is highly important is the issue of claims made after a change in insurance arrangements, or 'tail' claims. A major consideration for RSE licensees is to ensure that members whose claims relate to a previous contract with a prior insurer, are not inconvenienced due to any kind of lesser importance placed on these claims by insurers who are no longer in receipt of premiums from this policy.

To ensure that due regard is paid to claims against a policy which is no longer in effect, we recommend that paragraph 6(a) be amended to include addressing the issue of an insurer's philosophy and processes regarding their assessment of claims arising from being the previous insurer.

We would alternatively welcome a section that deals specifically with the issues associated with claims against old insurance contracts. Issues specific to these circumstances that need to be addressed would include claims rate, processes, reporting, liaising with new insurer, and the transition of data and ongoing provision of data to the new insurer.

Monitoring the RSE licensee and other relationships

We note that in *Prudential Practice Guide SPG 250 Insurance in Superannuation*, it is recommended that the relationship of RSE licensees with insurers requires frequent and appropriately resourced reporting. Similarly, this recommendation is made in the Draft Guide at paragraphs 23-25. We would welcome expansion of this paragraph, to ensure compatibility with paragraphs 43 and 44 of SPG 250.

AIST welcome's APRA's approach to the reporting of emerging experience is appropriate and we believe that trend analysis is important. We also believe that this paragraph could be expanded upon to include reference to examples of where issues identified have the potential to make significant changes to terms and conditions and consider that it is also important for the insurer to identify positive trends. Focussing only on adverse trends could potentially see premium prices adjust at the expense of the RSE licensee and its members.

Finally, we also note the requirement of RSE licensees to ensure that the appropriateness, effectiveness and adequacy of their insurance management framework is subject to a review every three years. Further expansion of paragraph 25 to explain this requirement would be of assistance to insurers.

Sustainability

AIST supports the consideration given in paragraph 11 to the beneficiaries of the policy, with respect to premium rates and other terms and conditions. We are concerned, however that attention is not directed to the cost to members of superannuation funds of things like, for example, short-term group insurance contracts.

We note that in the case of some funds and insurers, the cost of a tendering process can run, on aggregate, into tens of millions of dollars. We believe that this could be minimised, and point out that it is the members of superannuation funds who ultimately wear the costs associated with this. Where these terms are short, this can only serve to increase costs.

We point to the current climate where variety of issues has resulted in a series of sharply increasing insurance premiums. These issues include rate guarantee periods, the increased use of lawyers in handling disputes associated with insurance related payments from superannuation funds, increased claims, reduced availability of reinsurance, and compliance with the recently issued *Prudential Standard SPS 250 Insurance in Superannuation*. Whilst we understand that the Draft Guide cannot provide the answers to this issue, we believe that it should be designed with such issues in mind.

AIST supports sustainable insurance contract practices, and would support recommendations aimed at reducing premium volatility in the interests of increasing certainty for superannuation fund members.

AIST also has issues with the consideration of profit-sharing arrangements as listed at paragraph 13(f). Although APRA is not the regulator responsible for issues associated with conflicted remuneration, we believe that the notion of profit-sharing can only be supported where these are handled transparently, including in cases of savings due to economies of scale. Similarly, we point to the obvious potential for such arrangements to create anti-competitive distortions in the group insurance market.

As a consequence, we strongly recommend that such profit-sharing arrangements be totally transparent to all end users and to be passed through to members of superannuation funds in their entirety. This pass through could also be by way of service improvement, for example, covering the cost of insurance administration or improvement of insurance services in addition to reductions in premiums.

Outsourcing

We welcome the guidance that this document provides with respect to outsourcing operations that would be undertaken by insurers. Whilst we support the note at paragraph 21 that reinforces insurers' obligations under *Prudential Standard CPS 231 Outsourcing*, we wish to issue a reminder that the majority of business undertaken by insurers in the provision of group risk insurance is as outsourced service providers themselves. Consequently, whilst mindful of the requirements of insurers under CPS 231, we also wish to point out the potential that these requirements have to conflict with requirements for RSE licensees under SPS 231.

We cite as an example the guidance provided in paragraph 22, where insurers are advised not to outsource claims decisions. We believe that this has the potential to run contrary to what a trustee believes might be in the best interests of its members. We point out that the decision to pay a superannuation benefit due to death or incapacity is a decision that is generally made by trustees, and we support efforts to ensure that decisions are ultimately made in their members' best interests. It may be that in some instances, an insurer may choose to outsource claims decisions back to an RSE licensee or their agent. In these instances, a decision not to outsource may, in itself may be a sub-optimal outcome for the end users of the policy who are the members of a superannuation fund. Furthermore, we cite reinsurance practices which, in effect, outsource claims decisions back to insurers as a further example of where this business model is used effectively.

We consider that where a third party has the necessary resources and expertise to process claims decisions, we do not see why a practice of outsourcing shouldn't continue with appropriate monitoring, audit and risk management strategies in place.

AIST recommends that paragraphs 21 and 22 be viewed through the lens of RSE licensees' obligations under SPS 231.

Responding to a tender

AIST supports that the guidance in paragraphs 26 to 29 to be excellent guidance for both insurers and RSE licensees who initiate tender processes. In particular, we support the sentiments conveyed at paragraph 29, where APRA recommends that insurers should withdraw from a tender process, where the time allowed for a response is insufficient.

Data management

Paragraph 30 discusses the requirements under SPS 250 for RSE licensees to retain records of claims experience, membership, sums insured and premiums paid for the last five years. Although not necessarily required by SPS 250, we would support a recommendation for these records to go back further, noting that five years may not necessarily cover more than one contract with an insurer. We believe that this would further enable life insurers to assist the lifting of standards across the superannuation industry with regards to the retention of this information.

Data used in tenders

We are uncertain whether paragraphs 40 and 41 may be interpreted as being contradictory. On one hand, paragraph 40 recommends that insurers should make allowances for uncertainties to be contained in data presented to them. On the other hand, paragraph 41 recommends that the practice of insurers waiving their rights under the Contracts Act to take remedial action if data is found to be incomplete or incorrect.

We agree that a prudent part of responsible tendering is assuming a band of confidence in the data provided. However this work would appear to be wasteful if contractual rights may be asserted in the event of variances from the data that was originally presented.

AIST makes no recommendations with respect to these paragraphs other than to point out that a comment which reconciles these two paragraphs would be welcome.

If you have any further questions regarding this submission, please contact Richard Webb, Policy & Regulatory Analyst on 03 8677 3835 or at rwebb@aist.asn.au .

Yours sincerely,

Tom Garcia
Chief Executive Officer