Senate Economics Legislation Committee

ANSWERS TO QUESTIONS ON NOTICE

Treasury Portfolio

Additional Estimates 2020 - 2021

Division/Agency: Australian Prudential Regulation Authority
Question No: AET123
Topic: Questions for APRA on issues in relation to super funds and life insurance companies
Reference: Written (06 April 2021)
Senator: Slade Brockman

Question:

1. In a letter dated 9 March 2021 to Super fund and life insurance company CEOs, APRA mentioned emerging issues in the Group Super insurance market. I am particularly interested by the following words on tender practices, which seems to suggest that there has been some misconduct in this space:

"APRA has also observed increasing incidences of undesirable tender practices, including abbreviated timeframes for the tender process, or to respond to revisions in insurance design or other parameters as part of that process, being imposed; life insurers being unduly restricted by RSE licensees seeking to have a major role in determining the reinsurers that must be used; and the data provided being inadequate, out of date and/or not made available to all tender participants. These sorts of practices contribute to many of the issues outlined above, as they adversely impact the ability of life insurers to effectively and appropriately respond to the tender request."

Can you provide more context on the types of issues that you have seen, and whether there is any suggestion of illegality? If so, does APRA intend to take action and how?

2. With regards to issues on volatility in life insurance premiums: Have there been significant increases in premiums for many clients, including those who are now in legacy products and those products labelled as level premiums? What is APRA doing to protect the interests of these retail life insurance clients? Has APRA paid attention to the scale of some of these increases and if so, please outline the scope of these increases.

3. It has been reported that APRA's intervention into the Individual Disability Income Insurance market has made it much more difficult for small business owners and those who are self-employed to get income protection insurance. What is APRA doing to support the small business community that have been adversely impacted by these changes?

4. In April 2019, APRA and ASIC issued a joint letter to super fund trustees to highlight their responsibilities for the oversight of fees being charged by financial advisers, including the need to check that services are being provided. I understand that it has become common for super fund trustees to request documents from financial advisers to prove the provision of services, such as Statements of Advice, that could contain personal information that should not be made available to these trustees. To what extent is APRA aware of these practices and what steps have you taken to address the issue that the provision of such information by financial advisers might breach the privacy obligations? Has APRA provided guidance to trustees on what is appropriate information to request and how to address the potential issues with privacy?

5. Some life insurers have taken to offering upfront discounts in the first year or over the course of the first three years of a policy. Are existing clients indirectly paying for these 'discounts' by way of their large premium increases? If not, please provide some clarity on why premiums continue to spike for existing clients.

Answer:

1.

APRA's comments in the letter of 9 March 2021 were concerning industry practices that are not considered better practice or which may have unintended consequences, rather than being breaches of the relevant laws.

Tenders for group life insurance offered within superannuation can be quite complex. The sorts of issues that APRA was referring to in its letter include examples of tender participants (e.g. life insurers) being asked to produce quotations in quite short periods of time, and for multiple benefit configurations. This has a detrimental effect on the ability of the tender participant to properly allow for all relevant factors when constructing the tender response.

APRA has also been made aware that some tender consultants appear to have contributed to tenders unduly focused on price, with less consideration of other factors such as sustainable product design or service to policyholders. APRA's letter highlights that price should not be the only factor considered in tenders.

Other issues highlighted include RSE Licensees requiring insurers to use particular reinsurers. While this may be appropriate, in some cases this could lead to the insurer and reinsurer being mis-aligned in their claims philosophy and other practices.

APRA's letter also highlighted that the most up to date and fulsome data for tenders should be provided to all tender participants, and should meet the requirements of *Prudential Standard SPS 250 Insurance in Superannuation*. High quality and sufficiently granular data help facilitate sustainable insurance design and pricing.

2.

APRA's regular data collections do not include detail on premium increases for specific products, such as legacy products and level premium products. APRA is however aware of significant premium increases for broader product types, in particular disability income insurance products.

APRA has emphasised to industry the importance of disciplined and sustainable pricing, which is expected to contribute to providing policyholders with more certainty on future premiums. More sustainable pricing will also help to avoid intergenerational transfer of wealth whereby future policyholders pay higher premiums to compensate for unsustainable pricing of the past.

3.

APRA's understanding is that non-salaried individuals (such as small business owners and self-employed, whose income will typically fluctuate over time) have historically predominantly purchased Agreed Value individual disability income insurance (IDII) products.

For Agreed Value IDII products, the sum insured is set at the time the policy is issued and then remains unchanged, regardless of subsequent changes to the insured's income. This may result in the amount insured being very different to the customer's insurance needs, potentially resulting in situations where the insured is better off financially being on claim, compared with prior to the claim event. This sort of product design goes against the principles of sound insurance product design, and acts as a disincentive to sound 'return to work' strategies. It has contributed to the significant sustainability issues in the life insurance industry which have the potential to threaten the ongoing viability and availability of some types of insurance for the Australian community in the future. Issues with this sort of product design resulted in APRA requiring life companies to discontinue writing Agreed Value contracts from 31 March 2020.

While Agreed Value contracts are no longer available, APRA has set out measures for life companies to design IDII products with the necessary flexibility to meet the needs of non-salaried individuals. Indemnity IDII products should be an appropriate alternative for small business owners or self-employed individuals as this sort of product takes into account the average income over an appropriate period of time immediately prior to the disability, reflecting the future earnings likely to be lost as a result of the disability.

4.

The joint letter APRA and ASIC issued in April 2019 drew trustees' attention to the need to ensure they are satisfied that advice fees are deducted from member accounts only in circumstances where permitted by law; and the need for them to implement appropriate processes to ensure this is the case.

APRA and ASIC have engaged with industry bodies and individual trustees to understand the actions they are taking to fulfil this obligation.

We understand there is a range of practices employed by trustees in this area and APRA has not been prescriptive in describing how trustees should do this.

APRA and ASIC have continued to work together on this matter.

An update to the April 2019 letter is currently in preparation and will be issued in the next few months. This will provide more details as to the agencies' expectations.

Ultimately trustees must design and implement their own arrangements to ensure they are meeting their legal obligations in the best interest of members.

5.

Significant premium increases for existing customers are not related to upfront premium discounts for new policyholders.

Premium increases for existing customers generally arise from life insurers making premium adjustments to reflect claims experience, and in particular when they pay more out for claims than expected and priced for.

While there is not an inherent problem with providing policyholders with an upfront premium discount either in the first year or over the course of the first three years of a policy, APRA notes that it may not always be well understood by policyholders that they will experience premium increases when the upfront discount expires.

Upfront premium discounts are likely to be offset through other means, for example charging a marginally higher premium for the remainder of the contract, or through the profits on increased business volumes generated by offering the discount.