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Insurance in Super – a partial fix for under-insurance

ACFS releases roundtable report on “*Super: Implications for the Life Insurance Industry*”

The growth of superannuation has been significant for the structure of the life insurance industry, with most super funds offering standardized life and TPD insurance as automatic parts of their superannuation plans. For the life industry, it has meant an increase in group policies sold to super funds relative to individual policies, and has had implications for the levels of coverage and distribution mechanisms.

Minimum levels of life insurance must be offered in **employer-sponsored superannuation funds** under the SIS Act which governs fund trustees. The provision of life, total and permanent disability (TPD), and income protection insurance cover through super funds is now a big business for insurers. **With an aging population, and changes to remuneration for financial advisers, it is likely to become a more important business for financial planners within and outside of superannuation.**

Australian Centre for Financial Studies (ACFS) Director Prof Deborah Ralston states that *“insurance advice is one area where licensing of financial advisers may have had unintended consequences”*. For instance, most advisers and accountants who provide advice and administrative services to **self-managed super funds** are either focused on the investment and tax aspects. or on the insurance product itself. Tailoring for the life stage or risk tolerance of individuals may not be happening. Or if it, it may be that opportunities for tax deductibility (against contributions tax) are going begging.

Ralston noted that *“insurance coverage is wider than it would be otherwise without embedding it in super arrangements but there are significant public policy issues involved in the way insurance is offered in Australia. Issues include a significant lack consumer engagement, insufficient focus on insurance in financial advice, and under-insurance among those without superannuation.”*

The ACFS discussion paper notes that in employer sponsored funds, trustee determinations about the default level of coverage of their funds are important given the “behavioural biases which tend to lead to individuals not shifting from a default option”. A tripling of the default level by one scheme, while also giving members the right to opt out, was reported to have seen only one per cent opting out.

The ability of **super funds to now provide financial advice to members** is an opportunity for selling insurance. In so doing it raises questions about incentives and the nature of appropriate fee/commission relationships between the fund, insurance company and member. In not-for-profit funds any commissions will flow to the membership pool at large.

ACFS Research Director Prof Kevin Davis noted that *“With the impending ban on commissions from financial product providers, but an exemption from that ban for life insurance products, there may be enhanced interest shown by advisers in life insurance products.”* Because pricing of individual risk products is critically dependent on the personal characteristics of the individual mechanisms for assisting individuals (or their advisers) in choosing between competing supplier offerings are important. *“Whether this will be best served by insurance brokers or through web-based portals enabling individuals to seek bids from participating suppliers is another question”* Prof Davis added.

Davis concludes that *“income protection and TPD insurance are now sufficiently important to warrant being considered a compulsory element in superannuation alongside life insurance.”* He adds that *“so too may be trauma insurance”*.

The focus of the ACFS Financial Roundtable Report on **implications of Superannuation for the Life Insurance Industry** is beyond Chapter 5 in Part Two of the Australian Super System (Cooper) Review: Insurance in MySuper.

It identifies a range of issues worthy of further study:

- Is it significant that major life offices now have a more of their asset holdings in superannuation liabilities (wealth management) rather than in insurance?
- Given the different age composition of super funds, how optimal are current default insurance options?
- Whether the current structure of administrative arrangements and responsibilities between super funds and insurance companies in identifying member deaths and initiating claims payments is optimal.

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The full report is available at <http://www.australiancentre.com.au/publications-and-articles/2010/09162010-insurance-and-super-roundtable-report-frrs-2.pdf>

The *Financial Roundtable Report Series* assemble the expertise and thoughts of leading individuals on topics of interest to the finance sector. Through the use of roundtables, ACFS develops its thought leadership role by facilitating discussion among academics, industry practitioners, policymakers and regulators, to contribute to public policy debate and identify areas where further research is desirable.

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ACFS has established a Research Reference Group of academics, practitioners and regulators for Insurance. It has a key objective of building a dynamic insurance research agenda for academic staff and students to be of direct relevance to industry and government. Impetus for this ACFS discussion paper came out of that group.

The Australian Centre for Financial Studies (previously known as the Melbourne Centre for Financial Studies) is a not-for-profit consortium of Monash University, the University of Melbourne, RMIT University and Finsia having commenced in 2005 with seed funding from the Victorian Government. For more information: www.australiancentre.com.au

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