



Law Council
OF AUSTRALIA

Legal Practice Section

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By email: superannuation.policy@apra.gov.au

Dear Ms Squires

PROPOSED REVISIONS TO PRUDENTIAL STANDARD SPS 250 INSURANCE IN SUPERANNUATION

1. The Law Council of Australia welcomes the opportunity to make a submission to the Australian Prudential Regulation Authority (**APRA**) in relation to the proposed revisions to *Prudential Standard SPS 250 Insurance in Superannuation* (**SPS 250**). This submission has been prepared by the Superannuation Committee of the Law Council of Australia's Legal Practice Section (**Committee**).
2. APRA's proposed revisions to SPS 250 deal with four main matters:
 - recommendation 4.14 of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry (**Royal Commission**) (additional scrutiny for related party engagements);
 - recommendation 4.15 of the Royal Commission (status attribution to be fair and reasonable);
 - APRA's concern that some registerable superannuation entity (**RSE**) licensees have not given adequate consideration to the covenant in paragraph 52(7)(c) of the *Superannuation Industry (Supervision) Act 1993* (Cth) (**SIS Act**) (cost of insurance not to inappropriately erode the retirement income of beneficiaries); and
 - ease of opt-out of insurance cover.
3. The Committee would like to comment on the first three matters above (and two other, more minor revisions included in draft revised SPS 250).

Royal Commission recommendation 4.14 (additional scrutiny for related party engagements)

4. APRA proposed to implement this recommendation by making two insertions.

Paragraphs 24 and 25 – independent certification

5. First, APRA proposes to insert new paragraphs 24 and 25 as follows:
24. *An RSE licensee must obtain independent certification that an insurance arrangement, or any other arrangement entered into in relation to the provision of group insurance:*
- (a) is in the best interests of the beneficiaries; and*
 - (b) otherwise satisfies all applicable legal and regulatory requirements, where the insurance arrangement or other arrangement:*
 - (c) is with a related party insurer; or*
 - (d) gives priority or privilege to an insurer.*
25. *An RSE licensee that is required to obtain independent certification under paragraph 24 must provide the certification to APRA within five business days of its receipt by the RSE licensee and no later than one calendar month prior to the RSE licensee:*
- (a) entering into a new insurance arrangement; or*
 - (b) renewing an existing insurance arrangement.*
- If an insurance arrangement is for a term of, or exceeding, three years, the certification must be provided to APRA on a biennial basis.*
6. The Committee suggests that the certification in subparagraph 24(a) could be alternatively framed to the effect ‘that it is open to the trustee to form the view that the proposed arrangement is in the best interests of beneficiaries’. The advantage of this alternative formulation is that, while achieving the policy intent (in that a trustee could not enter into the arrangement without that certification), it clarifies and confirms that the best interests decision is one that is made by the trustee. Otherwise, it could be inferred from the above drafting that the responsibility for the best interests decision is being passed to the relevant independent certifier. This will also potentially avoid difficulties, from an insurance and liability perspective, for the independent certifier. The further advantage of this alternative form of certification is that it also permits the trustee to form the view (taking into account other relevant factors) that the arrangement is not in the best interests of beneficiaries. This determination would be very difficult for a trustee under the current absolute certification.
7. The Committee is concerned that subparagraph 24(d) is unclear and, therefore, the circumstances in which a trustee may or may not need to obtain independent certification (where the insurer is not a related party) will be uncertain.
8. The Committee acknowledges that the Commissioner used the words ‘by which the insurer is given a priority or privilege’ in recommendation 4.14 and appreciates that APRA has adopted virtually identical language. However, in order to understand what the Commissioner was concerned with, it is necessary to go back to the discussion in

the Final Report. That discussion focussed on related party insurers and 'questions of conflict', before continuing (emphasis added):

And because conflicts can arise not only from legal structure but also from contractual arrangements, the same obligation should apply to any RSE licensee that has a contract, arrangement or understanding with a life insurer by which the life insurer is afforded a priority or privilege in connection with the provision of group life insurance to the RSE licensee.

9. With the benefit of this context, the Committee suggests that the scope of subparagraph 24(d) should be refined by replacing the proposed text with:

gives, to an insurer that is not a related party, priority or privilege such as to raise questions of conflict of the kind that would be raised if the insurer were in fact a related party.

10. This would mean that 'priority or privilege' that did not rise to the relevant level would not trigger the requirement to obtain certification. Almost all insurance arrangements arguably involve 'priorities' or 'privileges' of one kind or another for the insurer and yet the Commissioner plainly did not intend that the certification requirement would be triggered in virtually all cases.
11. As a small point, the words 'where the insurance arrangement or other arrangement' in subparagraph 24(b) should be brought down onto their own separate line (without any paragraph lettering), or alternatively (c) and (d) should be subparagraphs of (b) (indented as (i) and (ii)).

Paragraph 18(n) – insurance arrangement to 'address' trustee's termination right

12. Secondly, APRA proposes to add to the list of matters that must be addressed in an insurance arrangement (in the paragraph proposed to be renumbered paragraph 18), by inserting a new subparagraph (n) as follows:

the RSE licensee's right to terminate the insurance arrangement, should an independent certification received under paragraph 24 be negative.

13. The Committee notes that, at present, few if any insurance arrangements will address, in terms, a termination right in the event of a 'negative' independent certification. Some arrangements (indeed, one would expect, many arrangements) would address that matter indirectly, by giving the trustee a termination right in the event that the arrangement was considered to be contrary to law or the trustee's duties. However, it would be preferable to refine paragraph 18(n) by replacing the proposed text with:

a right of the RSE licensee to terminate the insurance arrangement, should the arrangement not be in the best interests of the beneficiaries or otherwise fail to satisfy applicable legal and regulatory requirements.

14. The Committee anticipates that, in some cases, an insurance arrangement may need to be renegotiated in order to deal with the possibility of an adverse certification. The Committee suggests that APRA should consider amending its prudential standards for life companies to require them to allow a superannuation trustee to have appropriate termination rights, in turn to ensure that there are no barriers to trustees complying with APRA's proposed amendments to SPS 250.

Royal Commission recommendation 4.15 (status attribution to be fair and reasonable)

15. APRA proposes to implement this recommendation by inserting a new paragraph 19 as follows:

Any status attributed to a beneficiary (including a class or cohort of beneficiaries) in connection with the provision of insurance must be fair and reasonable.

16. However, the Committee notes that recommendation 4.15 is in these terms (emphasis added):

*APRA should amend Prudential Standard SPS 250 to require RSE licensees to be satisfied that **the rules** by which a particular status is attributed to a member in connection with insurance are fair and reasonable.*

17. The Committee suggests that what should be required to be fair and reasonable are (consistent with the text of the recommendation) the rules under which attribution occurs. Attribution of status that is not fair or reasonable (notwithstanding rules that are fair and reasonable) – for example, a mistaken attribution caused by a processing error – should not fall within the paragraph. That is not a scenario with which the Commissioner was concerned and such a scenario would be adequately dealt with by existing law, for example the duty of care, skill and diligence in paragraph 52(2)(b) of the SIS Act.

Cost of insurance not to inappropriately erode the retirement income of beneficiaries

18. APRA proposes to address its concerns in this respect by adding the words bolded to subparagraph (a) of the 'Insurance strategy' requirements in SPS 250 (proposed to be renumbered paragraph 16), under which the trustee must document:

*how the RSE licensee has regard to each of the factors in section 52(7) of the SIS Act, and **specifically how it has confirmed that the level and type of cover will not inappropriately erode the retirement income of beneficiaries;***

19. The Committee suggests that this amendment should not be made. Apart from anything else, the amendment unavoidably suggests that the covenant in paragraph 52(7)(c) is, somehow, more important than the covenants in paragraphs 52(7)(a) (formulate, review regularly and give effect to an insurance strategy), 52(7)(b) (consider the cost to all beneficiaries of offering or acquiring insurance) and 52(7)(d) (do everything that is reasonable to pursue an insurance claim). The Committee doubts that it is APRA's intention to make such a suggestion but it is, nevertheless, an implication that would inevitably be drawn if the amendment were to be made.
20. The Committee is not aware of any suggestion that paragraph 52(7)(c) is inadequate. APRA's concern 'that some RSE licensees have not been giving adequate consideration' to the covenant could, in the Committee's respectful view, be addressed in better ways than by singling out (and then essentially reiterating) paragraph 52(7)(c) in SPS 250.

Other

Maintaining records

21. APRA proposes to amend the existing requirement to maintain records (in the paragraph proposed to be renumbered paragraph 14) by inserting the words bolded below:

*An RSE licensee must maintain records of sufficient detail **to comply with its obligation under the prudential framework and** for a prospective insurer to properly assess the insured benefits that are made available. These records must include, for at least the previous five years, the claims experience, membership, sum insured and premiums paid in relation to beneficiaries.*

22. The proposed addition is unclear, with the obvious question being – which obligation? If APRA has in mind a particular obligation, it would be preferable for the obligation to be expressly identified. If APRA has in mind more than one obligation, again it would be helpful for them to be identified. Further, if the obligation (or obligations) APRA has in mind relates to record maintenance obligations, the words are redundant. If the obligation (or obligations) APRA has in mind does not relate to the record maintenance obligations (for example, the trustee's obligation to be able to satisfy itself that the engagement of an insurer is in the best interests of beneficiaries), then maintaining records that might be relevant to that obligation is something a trustee would otherwise already be obliged to do (for example, by its duty of care, skill and diligence) or would otherwise do in any event.
23. The Committee has been unable to identify anything in APRA's letter to RSE licensees dated 25 November 2019 (by which views on draft revised SPS 250 were sought) that explains the proposed amendment.

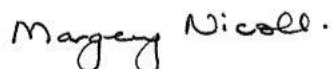
Transitional arrangements

24. Finally, APRA proposes to amend the 'Transitional arrangements' provisions by limiting them to the list of things that must be addressed in an insurance arrangement. The Committee queries this approach and suggests that they should be further limited, to the only item in the list that is new, namely, proposed new subparagraph 18(n), discussed above.

Contact

25. The Committee would welcome the opportunity to discuss its submission further and to provide additional information in respect of the comments made above. In the first instance, please contact the Committee Deputy Chair, Ms Natalie Cambrell at ncambrell@hwle.com.au.

Yours sincerely



Margery Nicoll
Acting Chief Executive Officer