

08/02/2022

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Superannuation
Australian Securities and Investments Commission
By email: SuperForecastsConsultation@asic.gov.au

Dear Ms Chew,

Consultation Paper 351 (CP 351) Superannuation forecasts: Update to superannuation calculators and estimates relief

Thank you for the opportunity to participate in this consultation on ASIC's proposals to amend legislative instruments relating to superannuation calculators and retirement estimates.

AustralianSuper is Australia's largest superannuation fund and is run only to benefit members. 2.5 million Australians are members of AustralianSuper and we invest over \$250bn of their retirement savings on their behalf. Our purpose is to help members achieve their best financial position in retirement, including through the provision of information and advice.

Like ASIC, we believe superannuation forecast tools are useful to support superannuation fund members and Australians more broadly by assisting them to engage and understand the long term investment horizon for superannuation, their particular circumstances now and in the future and how superannuation can be part of their retirement income.

Timing of related consultations

In preparing this submission, we note this consultation is occurring prior to Treasury's Financial Advice Review, which will likely include reviewing the legal definition of personal financial advice and general advice. Given CP351 provides relief from superannuation calculators and retirement forecasts being regulated as personal advice, but the scope of this consultation does not extend to the question of whether calculators and retirement projections should be considered personal advice or rather guidance or indicative outcomes, we recommend government ensure this question is captured in the Financial Advice Review.

AustralianSuper members' utilisation of calculators and tools

AustralianSuper provides a range of member engagement tools and calculators. Our most popular calculator is the Super Projection Calculator (SPC), followed by the contribution's calculator and insurance calculator. In FY21 there were over 200,000 users of the SPC. In FY22 the SPC is averaging 20,000 users a month. The SPC calculator is heavily used by our 55 to 59 and 60 to 64-year-old member cohorts, however there is still strong use by younger age groups (45 to 49; 50 to 54) and people over 65.

Response to Consultation

We support ASIC's proposal to give Trustees greater flexibility to set assumptions that reflect the types of products they offer and require greater consistency in the assumptions applied across superannuation calculators and retirement estimates. However, as set out below, we do not support all of Treasury's proposed assumptions set out in section C, namely C14 and C15, because this will produce confusing results for members.

We have also provided some specific answers to CP351 questions, where relevant, at the end of this submission.

1. Discount Rates (Proposal C14)

AustralianSuper supports the proposed approach for discounting prior to retirement (wage inflation). However, we disagree with the approach suggested for discounting after retirement (price inflation).

The different treatments afforded to the Age Pension and income from superannuation under the proposed approach are inconsistent and will cause anomalies and confusion for superannuation fund members.

To illustrate, we have provided a case study using the AustralianSuper Super Projection Calculator (SPC) using the following assumptions:

- A member retiring at age 67 with a superannuation balance of \$200,000 (in the absence of any further information on non-superannuation assets this member will receive the full Age Pension from retirement age),
- A retirement income target of \$40,000 per year (in real terms) from both superannuation and the Age Pension combined,
- A single homeowner for Age Pension purposes, and
- Notable price inflation of 2.5%pa, wage inflation of 3.5%pa and return assumption post-retirement of 6.0%pa net of fees and taxes.

Under the current Regulatory Guide:

- All income is assumed to increase in line with wage inflation (both from superannuation and the Age Pension),
- All future income is then converted to “today’s dollars” by discounting at wage inflation, and
- Note that wage growth is typically assumed to be long term 3.5-4%pa (as noted above the SPC defaults to 3.5%pa but the user can alter this).

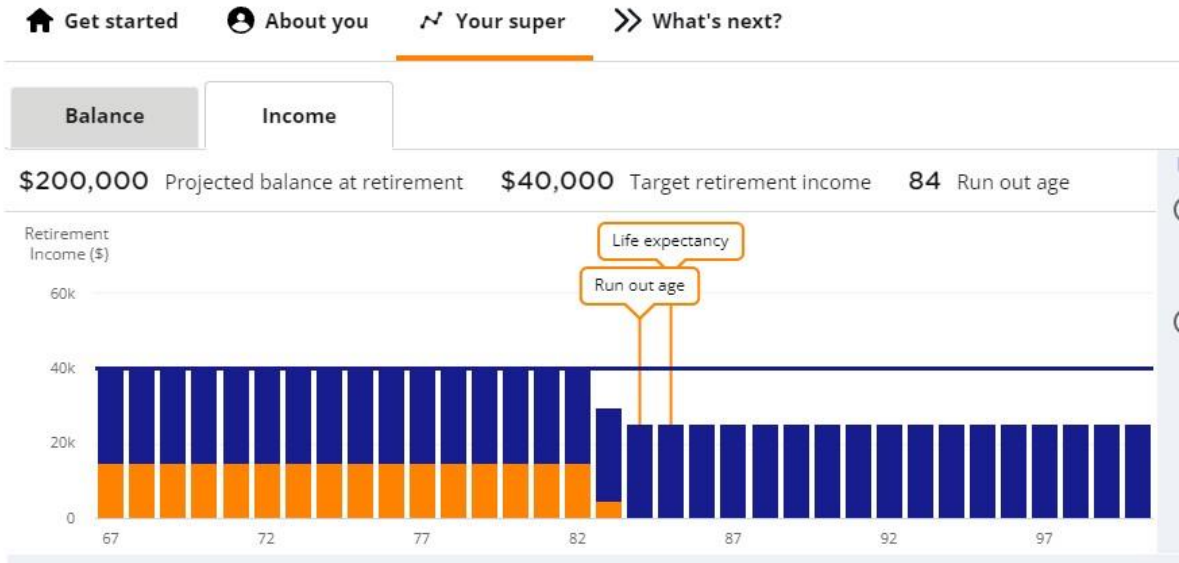
The results for this calculation are displayed in Chart 1. On current settings, this provides a simple and easy to understand graphic based on the retirement income target of \$40,000 per year in today’s dollars.

Namely:

- The retirement income target of \$40,000 is consistent,
- The proportion of the retirement income target met by superannuation drawdowns is represented by the orange bar (\$14,758pa),
- The proportion of the retirement income target met by the Age Pension is represented by the blue bar (\$25,242pa),
- This level of the retirement income target will last to age 82, with a final smaller drawdown at age 83 exhausting the member’s superannuation balance,
- From age 84 onwards the only income is from the Age Pension.

The benefit of this model is that members can see at a glance the income level, in terms of today’s purchasing power, they can expect to receive over “x” number of years together with an estimated impact of the Age Pension.

Chart 1: Retirement Income Graphical Representation – Current Approach

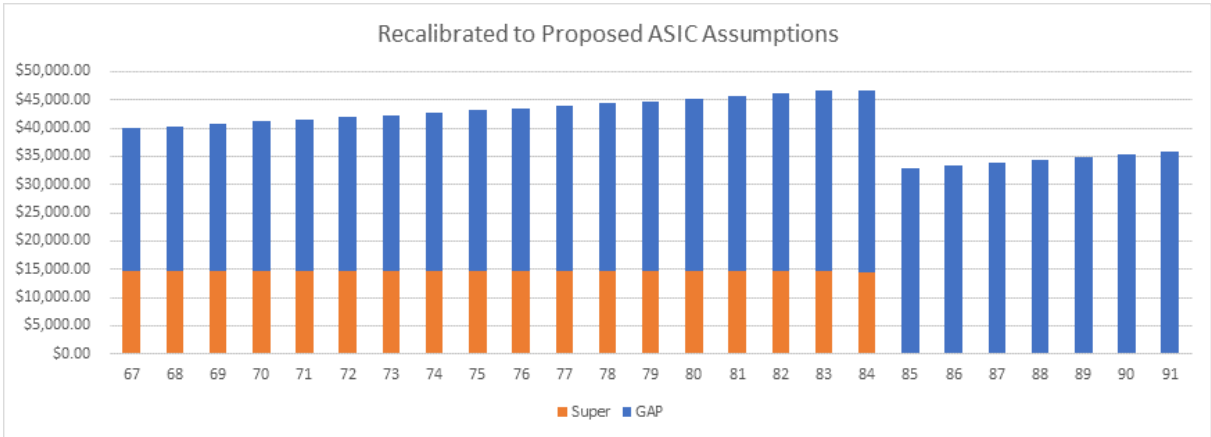


Under ASIC’s proposed approach in Proposal C14:

- Superannuation income is assumed to increase in line with CPI,
- The Age Pension is assumed to increase in line with wages growth (i.e. higher than assumed for super income),
- All future income is then converted to “today’s dollars” by discounting at CPI, and
- Note that CPI is typically assumed to be 2.5%pa, lower than wage inflation.

The chart below illustrates what happens to the graphic from Chart 1 if ASIC’s proposed assumptions are adopted.

Chart 2: Retirement Income Graphical Representation – ASIC’s Proposed Approach



We believe the proposed approach has the potential to cause confusion for members due to:

- Superannuation income stays at the same level but due to the use of (the lower) CPI in place of wage inflation in provides for an additional 2 years of income,

- However, the Age Pension looks to increase each year in nominal terms. This is due to the outworking of projecting income at a higher rate (wage inflation) to the deflator (price inflation), and
- As a result of the different assumptions users of the user cannot see that they will be able to maintain a desired annual income of \$40,000 across both sources of income. This could be alleviated by reducing drawdowns in each year of the projection such that, when combined with the Age Pension, income sums to \$40,000 in each year. However, the projection will still show an increasing Age Pension before and after super is fully drawn down.

For the user income is income, regardless of whether it is received before or after retirement, and whether it through superannuation or the Age Pension. A consistent application of assumptions is required to present users with a clear and consistent projection of their retirement needs. The Consultation Paper fails to outline why wage inflation is an appropriate assumption for the Age Pension, but not for superannuation income.

2. Wage Inflation at 4% (Proposal C15)

We recommend the use of a more conservative wage assumption than the proposed 4% p.a. We recommend using a wage inflation assumption of 3.5% pa as more reflective of the last 10 years' experience and is consistent with other government assumptions and previous ASIC advice.

Australian Bureau of Statistics (ABS) data

Over the long term, wage inflation has typically been in the range 1% to 1.5% p.a. above CPI. ABS data (6401.0 (CPI) and 6302.0 (Average Weekly Earnings)), indicates the margin of wage inflation above CPI has been:

- 1.08% pa over the 10 years to June 2021, and
- 1.48% pa over the 30 year period to June 2021.

This historical data is more consistent with an assumption of 3.5% pa.

Federal Budget Assumptions

Short term wage inflation assumptions used by The Treasury for the Budget Forward Estimates support a more conservative wage inflation figure.

Table 1 over the page sets out a summary of assumptions from the last seven Federal Budgets. These assumptions, reflecting the forecasts of the Treasury, show for each Federal Budget, the latest projection year and the wage increase assumption for that projection year. While short term assumptions, the latest projection year provides a good indicator for long-term assumptions.

Over the period presented below, the wage assumptions have typically been 3.5% p.a. or below. The most recent assumption (for FY24 set out in the last Federal Budget) has reduced markedly down to 2.25% providing some guidance of Treasury forecasts for wage inflation.

Table 1: Historic Federal Budget Assumptions

Federal Budget Year	Latest Projection Year	Wage Increase Assumption
FY15	FY18	3%
FY16	FY19	3.25%
FY17	FY20	3.50%
FY18	FY21	3.75%
FY19	FY22	3.50%
FY20	FY23	3.50%
FY21	FY24	2.25%

2021 Intergenerational Report Assumptions

The Consultation Paper indicates that the proposed wage inflation assumption of 4% pa is set to be consistent with the projections in the 2021 Intergenerational Report (IGR). This reflects the top end of historic long-term wage inflation. We contend it is not appropriate to rely solely on this source for all projections for the following reasons:

- The IGR is focused on systems growth, rather than individual member projections,
- All assumptions have been set without consultation with the industry. A survey of leading economists and assets consultants is likely to result in a more conservative figure, and
- The IGR contains a number of other assumptions that might not necessarily be appropriate. For instance it assumes that superannuation system will have the same structure in 40 years' time, a forecast that is required for IGR modelling simplicity but not reflective of sector change.

Impact on Past Projections

Many funds have adopted a wage inflation assumption of 3.5% pa in their online calculators, while some have used the prescribed 3.2% pa in accordance with ASIC Corporations (Amendment) Instrument 2019/514 that applied from December 2019. A move to a prescribed 4% pa will result in different outcomes that can render past projections invalid and cause confusion for users that have relied on previous projections.

Consider the following case-study results from the Fund's SPC:

- A member on median earnings (~\$74k) over a working lifetime (ages 25 to 67),
- Assumptions as set out in the SPC (including wage inflation of 3.5% p.a., a pre-retirement investment return of 6.5% p.a. net of fees and taxes and the SG rising in line with legislated increases).
- Variations to the wage inflation assumption – which also serves as the discount factor for expressing future values in today's dollars – results in the following divergent projected retirement lump sums:
 - Wage inflation = 3.2% pa – Projected retirement balance = \$595,000
 - Wage inflation = 3.5% pa – projected retirement balance = \$554,000
 - Wage inflation = 4% pa – projected retirement balance = \$492,000

A retirement balance projection on 3.5% pa wage growth assumptions yields an amount that reaches the ASFA Comfortable Standard (single, homeowner) of \$545,000. Altering the assumption to 4% pa now results in a shortfall of \$62,000. A member who has been tracking their super will suddenly see that their retirement plans are not being met. The difference is larger – over \$100,000 – altering the assumption from 3.2% to 4%.

Past Guidance – ASIC's Regulatory Guide 229

ASIC's Regulatory Guide 229 issued in November 2014 set out the following for superannuation forecasts:

“You must use the specified assumed rate of investment earnings—that is, the real (relative to wage inflation) investment earnings rate ... which is 3% per year.”

A CPI assumption of 2.5% p.a. plus an investment objective in our Balanced option (to exceed CPI by 4% p.a.) means we have a net investment return of 6.5% p.a. for the majority of our projections. If the wage inflation assumption is set at 3.5% pa (and used as the deflator to offset future inflation), the real return that emerges from this is (approximately) 3% (6.5% less 3.5%), which conforms to the previous ASIC Guidance.

If the wage inflation assumption is increased to 4%, the real return will reduce to approximately 2.5% p.a., which appears low. Superannuation funds have earned a median return of 7.33% p.a. over the 20 years to 30 June 2021¹. Over the same period wage inflation has been 3.8% pa (source: ABS publication 6302.0), resulting in a real return of approximately 3.5% pa. Accordingly, we would suggest that real returns should be closer to 3% pa in the assumptions set, better achieved by a wage inflation assumption of 3.5% pa.

Consistency with Past Guidance - ASIC Corporations (Amendment) Instrument 2019/514

Given ASIC previously prescribed a 3.2% pa wage inflation assumption in 2019, an increase to 4% pa in 2022 when wage growth has been low in recent years is counter-intuitive.

If ASIC's new guidance is followed, and using the example set out above for a median earnings worker over a working lifetime, illustrative comparative members would have seen the following changes to their projected retirement balance:

- Wage inflation at 3.5% pa – projected balance = \$554,000
- Alter wage inflation to 3.2% pa from December 2019 – projected balance increases to \$595,000
- Alter wage inflation to 4% pa in 2022 – projected balance decreases to \$492,000

A further outworking of these examples – which are pre-retirement only – is that the CPI assumption does not impact the calculation. This allows assumption setters to focus on the wage inflation assumption and the actual and real investment return. It also makes it easier to illustrate how changes in wage inflation assumption can alter retirement balance projections significantly. The same is true for post-retirement projections. However, the introduction of the CPI as a deflator complicates matters and potentially masks final results. This is a further adds to the argument for maintaining a wage inflation deflator post-retirement.

¹ SuperRatings Fund Crediting Rate Survey at 30 June 2021, SR50 Growth (77-90) Index)

3. Further Specific responses

We have commented on selected specific questions from CP315, where relevant.

C4Q2. How frequently should providers be expected to revise the economic and financial assumptions they apply?

We revise our assumptions annually and have done so since 2014. We do note that these assumptions are long term in nature and (in respect of economic assumptions) expect that these should only be altered if there is a material change in economic circumstances that impacts the long term. Constant changes can lead to consumers not understanding or valuing projections. Assumptions relating to fees and insurance premiums are changed as and when they happen.

C5Q1 Should trustees be expected to set the same assumptions across all superannuation calculators and retirement estimates they provide? In what circumstances should assumptions be able to differ?

Transition to Retirement Calculators are different as they have a shorter-term focus.

C6Q4 What guidance should ASIC provide on how assumptions about investment earnings, fees and costs should be set? Would it be appropriate for trustees to set assumptions on the basis of existing investment return objectives for superannuation products they offer (e.g. the return objective disclosed in the Product Disclosure Statement (PDS) or set by the trustee board?)

Most funds have investment options with investment objectives linked to a margin above CPI. AustralianSuper's default Balanced option (where 90% of the Fund's members are invested) has the objective to exceed CPI by more than 4% pa over the medium to longer term. With a CPI assumption of 2.5%, this lends itself to a long-term return assumption of 6.5% p.a. (2.5% + 4%).

ASIC's current guidance under section 6(1)(a)2016/207 (Generic Calculators) could be enhanced to qualify what constitutes the advertisement or promotion of a specific product. Return assumptions that are anchored to the specific objectives of particular investment products, would enable trustees to provide more meaningful projections to members. Currently, default assumptions may be loosely based on these objectives, however trustees are unable to explicitly connect these assumed returns to their product's investment options, making it difficult for members to take positive actions in relation to retirement outcomes.

C7Q3 Should we allow or require trustees to set different default assumptions for administration fees in the accumulation and retirement phases when working out a retirement estimate? Why or why not?

Yes. These tend to be different as each will have different internal operating structures. This translates into different default assumptions in calculators, and members should be made aware of them, so they expect a fee change when converting from the accumulation phase to the pension phase.

C10Q1 For retirement estimates, what additional assumptions would need to be made to work out the annual income stream in the way that we propose? Should ASIC prescribe a specific formula? Why or why not?

With respect to a static superannuation projection, we prefer a 25-year drawdown to a zero account balance. Further, our preference is to also allow for the Age Pension in determining an indication of the level income that could be expected over this drawdown period. Under the current approach, we prefer not to disclose the expected first year's Age Pension. As the retiree's balance is drawn down, they will become eligible for more and more Age Pension over time. So the initial Age Pension is not indicative of what the retiree may eventually receive over time. An alternative would be to allow for the average annual Age Pension expected over the 25 year drawdown period to be disclosed.

However, for an interactive projection, a more flexible approach would be necessary to enable the retiree to visualise the change in income levels over time. In turn, this empowers the retiree to make a more informed decision about the precise level of income to draw from their superannuation in the early years of their retirement and supplement their initial Age Pension benefits.

C11Q2 Should age pension amounts be required by default in interactive retirement estimates or in superannuation calculators? Why or why not?

We believe this is appropriate as members should be given an indication of what they can expect from known income sources. The SPC also allows for the ability for the member to refine the Age Pension estimate with further information on home ownership status, married/single, non-super assets, etc. Members also have the ability to switch off the Age Pension information.

C12Q1 Are there other ways in which assumptions could be made about future superannuation contributions in working out retirement estimates (e.g. using a three-year rolling average)? To what extent would this better reflect how contribution levels may change over the long term for most members?

Three-year averages will understate in times when the SG is going up. Instead we would suggest using the previous year's contributions ratioed by the increase in SG from the next year to the last. If past contributions look "lumpy", ASIC could allow the ability to examine a three-year average if this will provide a more meaningful projection.

Thank you for opportunity to make submission. If you would like to discuss any of the aspects raised in this submission please me on.
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We are also happy organise a discussion with AustralianSuper's actuarial team if that would be helpful to ASIC.

Kind regards

Nick Coates
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