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Mr J Cooper  
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Super System Review  
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Dear Mr Cooper

## AUSTRALIANSUPER SUBMISSION TO SUPER SYSTEM REVIEW

This submission includes comments on the following papers released by the 'Review Into the Governance, Efficiency, Structure and Operation of Australia's Superannuation System' (Review):

- (i) Phase One – Preliminary Report Clearer Super Choices: Matching Governance Solutions, and
- (ii) Phase Three – Structure Issues Paper.

AustralianSuper has had input into other material you will receive on both documents, and rather than duplicate those view the purpose of this paper is to highlight matters of particular interest to this Fund on behalf of our members. Before doing so it would be useful to make some general comments and briefly outline our conceptual view of the framework of the superannuation system.

### General Comments

We support the comments made by the Federal Government at the time of the announcement of the Review about the overall foundations of the superannuation system. We believe that the fundamentals of the system are sound, but that there remain significant opportunities to improve its operation so that it delivers better results for fund members.

### Framework

We believe that the superannuation system has a number of characteristics which mark it as different from most other industries, and that these factors should influence the behaviour of those parties regulating and working in the system.

- 1 The unusual characteristics of the industry include:
  - a. The superannuation system is compulsory – most workers and most employers have to participate;
  - b. A significant proportion of fund members are currently not fully engaged with their superannuation account;
  - c. The system performs a vital public policy role as part of Australia's retirement income system; and
  - d. The system exists only because of Federal legislation. If the taxation concessions and the SIS legislation – both creatures of the Federal Parliament – were not in place there would be no superannuation system in its current form.
- 2 These features create two sets of obligations:
  - a For Governments and regulators – an obligation to ensure that the system operates as efficiently as possible in the interests of fund members; and
  - b For providers of superannuation services – an obligation to be mindful of the privileged position of the industry and the vital role it plays in the nation's

retirement income system. This should place an onus on superannuation fund trustees to focus on the interests of consumers (fund members) rather than their operating organisations. For the reasons outlined above this is a more significant issue in this industry than most others.

## **Phase One – Preliminary Report**

### Choice Architecture Model

One of the key findings of the Review is that the system is more costly and less efficient than it needs to be, due in part to the excessive regulation and complexity (much of the latter not being imposed by the regulatory framework) in the system. The Review suggests that the system can be improved to operate more favourably in the interests of members of funds.

AustralianSuper agrees with this thesis. However we do not support one of the means suggested in the report to address it, ie the proposed Choice Architecture Model for the superannuation system. The broad delineation of funds into: Disconnected / Universal / Choice / SMSFs does, at a high level, accord with four sorts of superannuation fund members.

However, there would be a number of significant practical issues associated with the proposal that means that, if implemented, a large proportion of fund members would be worse off. These include:

- (i) it is currently impossible to divide on the one hand the many millions of superannuation fund members who are in a default (Universal) fund because they are disengaged and have not made a choice, to on the other hand those whose level of engagement may range from moderate to high, who are also in a default fund having made a conscious decision to do so.
- (ii) Implicit in this model is that those who change funds are “engaged”. In fact most people who change funds do so because in changing jobs they are moving to an employer with a different default fund to the one at their previous workplace. This is not member engagement at work – rather the reverse.
- (iii) This model may entrench many members in a low-engagement model, with reduced member communication and consequent lower longer-term prospects of a higher level of engagement. It is possible that such funds could become “second-rate” superannuation funds with lower levels of service and performance. For example it is not clear why members of universal funds should have a low-risk investment orientation, with the consequent likelihood of lower long-term performance, as well as lower costs.
- (iv) The transition costs from the current model in which more than 10 million Australians operate would be massive, with little obvious benefit beyond that available through the existing models of large-scale and efficient member-oriented funds.
- (v) The suggestion that the Universal option would mandate lifecycle investment options is not supported. There is still massive debate about whether the apparent appeal of embedded advice in the form of lifecycle options is positive for members. AustralianSuper has recently conducted a major review of our default option and determined that the preferred outcome for our members is to retain the Balanced investment option for accumulation members.
- (vi) AustralianSuper supports the Review’s focus on reducing costs. However this model is unlikely to reduce costs for most members. In the case of AustralianSuper the costs in the Choice option would balloon as those members lost the economies of scale in administration fees afforded to them by the larger number of “Universal” members. And the investment costs for the “Universal” members would increase because the smaller number of “Choice” members contribute a disproportionately large amount of assets to the Fund’s overall asset base. Hence under this model we estimate that costs for both groups would increase due to the reduction in economies of scale.

Consistent with the Review's analysis of the superannuation system and the objective of improving the system in the interests of fund members we believe the Review should also consider:

- (i) mandatory electronic transfer of data and money from employers into the superannuation system, and for transfers within the system;
- (ii) use of a member's Tax File Number for member identification purposes;
- (iii) adoption of a revised model of taxation concessions as proposed in the ISN submission;
- (iv) removal of the \$450 monthly earning threshold for SG purposes;
- (v) allowing catch-up voluntary contributions based on certain eligibility criteria. This may include the following sort of conditions; beyond a certain age (say, 50); capped at a higher level than currently (say \$100,000 pa); and only open to people with an account balance below a certain level (say \$500,000).;
- (vi) removal of commissions and like payments from the remuneration structures of financial advisers and imposition of a "best interests" test applying to those who provide financial advice.

### Phase Three - Paper

- (i) Indigenous Australians (Section 13.1)

There are ways in which the superannuation system could better accommodate the needs of indigenous Australians, in particular in relation to insurance. Aside from various product initiatives that the industry is working on, the administration of insurance claims including identification issues works to the disadvantage of many indigenous Australians. This is particularly so for those living in remote parts of Australia.

The freeing-up of formal identification requirements (when much of the standard legal documentation is not available) would streamline the system in the interests of those eligible for benefits.

A differentiated preservation age reflecting lower life expectancy for indigenous Australians is also worthy of consideration. If a different preservation age was introduced it should be reviewed periodically and increased in line with increases in life expectancy.

- (ii) Allocation of members to default funds: role of industrial awards

The industrial relations system is clearly the best structure for the nomination of default superannuation funds at workplaces. The active role played by employer organisations and trade unions representing employers and employees respectively has seen the interaction of the superannuation and industrial relations systems operate to provide excellent outcomes for members.

Fair Work Australia has scheduled a review of awards to occur in 2014. Given that the modern award process has just been completed after a very lengthy and comprehensive process, the planned review would be the appropriate time to consider this issue.

- (iii) Capital Requirements

It is important here to identify the principal issue. It is not that superannuation funds should hold an arbitrarily determined amount of capital. Rather the issue is that funds should have a good understanding of their operational risks, and have appropriate mechanisms in place (including access to money) to manage them.

The existing capital requirements are appropriate. However APRA should formally ensure that superannuation funds regularly undertake appropriate risk assessments, and that they have ready access to sufficient money (including in an Operational Reserve) that can be deployed in the event that it is necessary to do so.

## Summary

AustralianSuper believes the nation's superannuation system generally operates well and in the interest of fund members. However we recognise that there are material opportunities for improvement, and we agree with the Review's assessment that different levels of member engagement warrant consideration of different models of service delivery. Key elements of the system such as high-performing default funds; sound default settings within funds; intra-fund advice; and "incorporation by reference" in communication materials, are examples of elements of the current system that accommodate varying levels of member engagement. These elements would be enhanced by a ban on commission-remunerated financial advice and an obligation on advisers to act in the best interest of their clients. The proposed Choice Architecture Model is opposed.

AustralianSuper's other contributions to the Review including those concerning costs, regulatory changes, and efficiency measures would all serve to improve the operation of the system from the perspective of fund members.

Regards

A handwritten signature in black ink, appearing to read 'Ian Silk', with a long, sweeping flourish extending to the right.

**IAN SILK**  
Chief Executive