



AUSTRALIAN INSTITUTE of
SUPERANNUATION TRUSTEES

**Response to issues paper:
*Superannuation: Assessing
Competitiveness and Efficiency, July 2017***

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AIST Submission to Productivity Commission

Response to issues paper: Superannuation: Assessing Competitiveness and Efficiency, July 2017

AIST

The Australian Institute of Superannuation Trustees is a national not-for-profit organisation whose membership consists of the trustee directors and staff of industry, corporate and public-sector funds.

As the principal advocate and peak representative body for the \$700 billion profit-to-members superannuation sector, AIST plays a key role in policy development and is a leading provider of research.

AIST provides professional training and support for trustees and fund staff to help them meet the challenges of managing superannuation funds and advancing the interests of their fund members. Each year, AIST hosts the Conference of Major Superannuation Funds (CMSF), in addition to numerous other industry conferences and events.

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Executive summary

In brief:

This submission reiterates AIST's strong support for the legislated but not yet implemented system for selecting default superannuation funds. Even without the enhanced quality filter arising from the legislated system, the existing model has delivered out-performance for default members and provided many benefits to the greater economy. The review process has failed to deliver any hard evidence that any of the proposed alternate models will deliver superior retirement outcomes for members. Without such evidence – and noting the risk and costs that would result from dismantling the current system – the Commission should be reluctant to recommend to the Government any changes that cannot be proven to lead to better retirement outcomes for members.

Inappropriate timing: The Government has directed the Productivity Commission to undertake this review three years earlier than recommended by the Financial System Inquiry. AIST questions the rationale to review the default fund selection process at a time when Budget policy changes and other reforms are still being implemented. Notwithstanding the delivery of some very positive reforms, the relentless reviews and reforms to superannuation has imposed large direct costs on funds while at the same time distracting strategic focus of boards and executives from further pursuing member interests.

Insufficient regard to current reforms: AIST notes that there are many reforms that are still to be fully implemented (such as SuperStream, the higher standards and accountability of MySuper products) that have already – and will continue to have – a major impact on system-wide efficiency, including the current default system. These have largely been ignored or under-valued by the Commission in assessing the competitiveness and efficiency of superannuation. More recent reforms announced by APRA, such as the outcomes test, will have direct impact on the Commission's considerations. In this context, AIST is concerned that the Commission appears to be promoting radical structural reform without regard to these major reform initiatives that have already delivered billions of benefits to members, and that promise increasing benefits over time. Change that does not have regard to existing reforms would be disruptive and damaging to fund members, the superannuation system, to the community and economy as a whole.

Existing default system has delivered superior outcomes: AIST strongly endorses the existing legislated arrangements for a quality filter of default superannuation funds to be applied by an expert panel of the Fair Work Commission (FWC). The failure of the Government to appoint Expert Panel replacements at the FWC has delayed the introduction of an important extra layer of

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consumer protection. Consumers would be better served if steps were taken to allow the additional quality filters to be applied to the default fund selection process.

Existing default system minimises system-wide costs: The existing industrial-based default system is a highly efficient distribution system, where member costs are close to zero and employer costs are low in that employers are selecting from a limited selection of funds. Equally, the costs to government are very low, including the indirect cost saving from a high-performing well-managed default system that means age pension outlays are lower than if the system was not as successful.

Evidence does not support a consumer-led market: The findings of behavioural economics – particularly in regards to inherently complex products – points to policies based on the theory of a consumer-led market failing super fund members. The emphasis of the Commission, the Government and the commercial retail funds in promoting such a market is ideological and could harm a great majority of fund members who are currently well-served by the existing MySuper default arrangements.

Lack of appropriate data standards makes comparisons difficult: Despite the intention of MySuper enabling easy comparison between funds, this is not always the case. The inclusion of complex lifecycle investment options in a simple, default product has made comparability difficult. This has been compounded by variations in the types of fees, insurance offerings, declared risk appetites and strategic asset allocations.

Comparisons in Choice sector even more difficult: There are numerous exemptions, gaps and inconsistencies in the regulators' reporting standards afforded through the legislative environment to Choice superannuation products. This not only promotes system-wide inefficiency, it severely limits the ability of members to compare MySuper products with Choice products and means members of commercial retail funds remain extremely vulnerable to being flipped from a MySuper product into inappropriate Choice products that are more profitable for the provider, and lower performing for the members. This submission identifies cases where trustees in commercial retail funds have manipulated data and reported zero or near zero investment fees.

Excessive choice generates market inefficiencies: Existing policies which facilitate the offer of an unrestricted number of investment options across APRA-regulated funds, and which place minimal barriers for the creation of SMSFs, generate material inefficiencies within the superannuation system as a whole. These inefficiencies have been largely ignored by the Commission.

Defaults no place for under-performing funds: AIST would support a process for the removal from modern awards of funds which substantially underperform their nominated risk and return objectives over the four year review period, and whose MySuper product provides below median net returns to members for that time. Importantly, that process should include consideration of

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funds to which an employer may make contributions under an award because of grandfathering. The recommended – but yet to be implemented – Fair Work Commission quality filter on products permitted to be offered as defaults would provide further safeguards against default members being placed in underperforming funds.

Alignment of funds with industries adds efficiencies: The alignment of funds with particular industries through the award-based determination of default funds provides the opportunity for a deeper and more predictable knowledge of the member base in order to design MySuper, other Choice investment options and insurance offerings tailored to the needs of a fund's demographic.

Flawed approach: The Productivity Commission's assessment of competition and efficiency within the superannuation industry has not had sufficient regard to differences between the three key sectors of the industry: profit-to-member, commercial retail and self-managed super fund sectors. AIST considers that the Productivity Commission has undertaken this review with a preferred starting position of a changed mechanism for deciding default funds, without proper consideration of the existing system or the improved, legislated but unimplemented system. AIST rejects the unsupported stance of the Productivity Commission, that judicial arrangements are not subject to accountability, and considers this stance to be further demonstration of the Commission's view of the existing legislated model of default fund selection. The refusal to sufficiently consider the existing system greatly reduces the value of the inquiry, and may adversely impact perceptions of the Commission as an independent body.

Response to criteria: This submission also contains AIST's updated review of the Productivity Commission's recommended criteria to assess the competitiveness and efficiency of superannuation. Out of the 115 proposed criteria we support 58, have reservations on 45 and do not support 12 criteria.

Introduction

Timing of the review

The superannuation industry is of strategic importance to Australia's current and future well-being. The availability of a deep and liquid pool of capital - now valued at more than \$2.1 trillion or one and a quarter times annual GDP – helped Australia weather the Global Financial Crisis. We invest in Australian companies and Australian infrastructure, as well as being a global investor.

Super fund members face a more comfortable retirement than they could achieve through the age pension alone, while government pension outlays are expected to be much lower than would be the case in the absence of superannuation.

The challenge for AIST and other proponents of the profit-to-members ethos in superannuation is about promoting members' best interests and maximising their retirement outcomes. Our members' objective – as reflected in this submission – is to pursue this approach notwithstanding an environment of never-ending change and increasing complexity.

The achievements of the superannuation industry have not come without difficulty. The industry has been in a continued state of change since at least the 1997 Wallis Inquiry. It has consolidated; we have many fewer but much larger funds.

Many of the changes have been as a result of government policy change, implemented following extensive consultation with the superannuation industry. They have had the result of increasing efficiency and focus on members' best interests. In recent times:

- SuperStream as a joint industry/government process has already delivered administrative efficiency gains for members, employers and funds estimated at \$2.4 billion a year, with these benefits increasing as SuperStream matures and is used as the basis for further initiatives. The on-boarding process for employers effectively only concluded in October 2016, and the current compliance rate is already in excess of 95%. The further initiatives include improved on-boarding of new employees, more frequent reporting and visibility of individual superannuation details, and ever-improving enabling services, e.g. new SMSF verification service.
- Savings in administration costs generated by SuperStream have been used in part to offset increases in costs per account due to the decrease in the number of low value accounts consequent on account consolidation measures.
- MySuper changes are not fully bedded down. After a five year transition period, and only since July 2017, all default monies are now in MySuper accounts. Members with a MySuper interest receive the benefits of the higher standards applicable to these accounts.

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- APRA data reporting, and subsequent analysis and publication, has not yet been fully implemented. Increased provision of data and its public visibility was intended by the Super System Review and successive governments to be a cornerstone of a more efficient and competitive superannuation system. For example, APRA has been developing a Data Dissemination Tool to assist with the analysis and greater understanding of superannuation data – but implementation is still a couple of years away.
- Unless deferred yet again, Choice Product Dashboards to complement the existing MySuper Product Dashboards will be implemented from 1 July 2019, along with new and comprehensive Portfolio Holdings Disclosure requirements from 1 January 2020. These should be implemented and allowed to operate for a reasonable period.
- Changes for fuller reporting to better facilitate a member driven market for those willing and able to participate in one have not yet been agreed as part of ASIC’s consultations on Regulatory Guide 97 (RG 97), let alone implemented.
- Legislated enhancements to the FWC process for the selection of default superannuation funds have been in limbo since 2014. This is a result of the government not completing the process of appointing an expert panel to assist with the selection of default funds. The improved process would increase the visibility, accountability and competitiveness of the selection process, and should be implemented as a priority.
- Further changes (with broad industry support) forthcoming with the proposed *Treasury Legislation Amendment (Improving Accountability and Member Outcomes in Superannuation) Bill 2017* will directly impact matters being canvassed by the Productivity Commission. For example, proposed outcomes assessment and public reporting in relation to MySuper products (in place of a test as to whether members are disadvantaged by a lack of scale) should strengthen the system overall, as will APRA’s proposal to extend that approach to Choice products as well as MySuper.

AIST considers that there needs to be a fair chance for each of these processes and new requirements to demonstrate their effectiveness, while also noting that the Financial System Inquiry, appointed by the current Government and chaired by David Murray, recommended that change should not be considered until 2020, by which time the MySuper reforms would have had the opportunity to mature and be assessed.

In this context, AIST is concerned that the Commission appears to be promoting radical structural reform without regard to these major reform initiatives that have already delivered billions of benefits to members, and that promise increasing benefits over time.

Change that does not have regard to existing reforms would be disruptive and damaging to fund members, the superannuation system, to the community and economy as a whole. While

recognising the benefits of a benchmark assessment of the system, the Commission's wider change agenda (e.g., in relation to default fund selection) is not accompanied by evidence that change would be in the interests of fund members.

While we appreciate the need to always be looking to continuous improvement, AIST cautions against change that is not supported by evidence and which will impact industry, members and the broader system in an untested way that could lead to detrimental outcomes.

Flawed approach in the Productivity Commission's positioning

AIST is deeply concerned by the approach taken by the Productivity Commission in its review to this point.

While recognising that the Commission is bound by the terms of reference it receives from government, AIST considers that the Commission's approach has been at different times either complacent (for example "The Commission considers its assessment framework to be comprehensive and robust") or combative (for example "From this perspective, the Inquiry has managed to unite the superannuation industry against the Inquiry's potential contemplation of more-than-incremental reform. A healthy dose of scepticism would suggest that there must be rents to be recovered for the benefit of members for such unanimity to be valid").

An alternative assessment, to which we would subscribe, is that there is widespread opposition to proposed reforms which are poorly thought through and unsupported by evidence.

We understand that the superannuation industry is of massive importance to Australia at many levels – as a stable long term investor in the Australian economy, as the custodian of deferred wages for its members and as a critical factor in determining their well-being in retirement, and as a major source of both taxation revenue and tax expenditure for government.

At the same time, we acknowledge the divisions in the industry between (1) industry, corporate and public sector funds (collectively, profit-to-member funds); and (2) commercial retail funds: and between (1) APRA-regulated funds collectively and (2) the self-managed superannuation fund (SMSF) sector.

We consider that a proper assessment of competition and efficiency within the superannuation industry needs to show a higher regard to differences between these groups than the Commission has done to date. AIST highlights some areas considered later in this submission.

Particularly in its discussion of the identification of default funds and the process for allocation of members to them, the Commission has taken a partisan stance adverse to the interests of profit-to-member funds and their membership. The Commission appears to have paid little regard to

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the current default process nor, more importantly, to the augmented process which has been legislated but not implemented due to failure on the part of the current government to fill positions on an expert panel of the FWC.

As discussed in more detail below, the Commission's adherence to a model of a consumer driven market in superannuation is not justified on the evidence, yet clearly colours its findings to date and fits far more comfortably with the business model of the commercial retail sector than with profit-to-member funds.

That preference appeared to influence the design of the member survey commissioned as part of the Productivity Commission second report, and the conclusions drawn from it.

Material regulatory impediments to competitiveness and efficiency

The fallacy of the member-driven superannuation market

There is significant research from behavioural economics supporting the view that a consumer-led market in superannuation is bound to fail, especially for younger and low balance members. When the benefits of a “purchase” are unclear and long deferred, and the present amount at risk is small, the cost of member search will far outweigh the perceived benefits, taking into account the inherent uncertainty in investment returns and effects of costs. When this is combined with strategies in place at some funds to make offerings less comparable, continuous changes in government policy mean that what you see now is definitely not what you get in 30-40 years’ time. It is far from clear that members will have the incentive to act in their own best longer term interests.

For example, Keane and Thorp note:

To make good retirement savings decisions, consumers need both: to know and understand the attributes of the products/services they are evaluating; and to possess the cognitive capacity and skills to make good choices among those products/services. [Consumers] are likely to become confused if they don’t have the facts about investment returns, survival, pension plan structures and government support to hand. They also need the basic numeracy, financial literacy, patience and personal efficacy to design and implement a plan. Empirical studies have highlighted both misperceptions about the key facts and serious deficits in the capacity of many people to make a plan and follow through.¹

The Cooper review noted

A key tenet of the 1997 Wallis Report was that super fund members should be treated as rational and informed investors, with disclosure and market conduct controls being the main regulatory instruments with which to oversee the industry.

More specifically, these settings assume that members have the tools at their disposal, and the necessary regulatory protections in the market place, to enable them to make optimal decisions about their investment strategies, about when to enter and exit the market, and

¹ Keane, M. and Thorp, S. (2016). *Complex Decision Making: The Roles of Cognitive Limitations, Cognitive Decline and Ageing*. Prepared for The Handbook of Population Ageing, Elsevier, J. Piggott and A. Woodland (Eds.). Revised 9 September 2016. [online] p.28. Available at: <http://tinyurl.com/y83ds3pv> [Accessed 18 Aug. 2017].

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about what to do with their super on reaching retirement. In a compulsory system, it also assumes that members have the requisite degree of interest.

But, for many members, this is not the case.

The 2006 Adult Literacy and Life Skills Survey of Australians published by the Australian Bureau of Statistics (ABS) in January 2008, found that 46 per cent of 15-74-year olds, or some seven million people, would struggle to understand documentation such as job applications, maps and payroll forms. Fifty-three per cent of surveyed Australians reached just the second of five levels in a practical numeracy test, while 70 per cent (about 10.6M people) managed only to progress to level 2 in a series of problem-solving exercises. Level 3 is regarded by the survey developers as the minimum required for individuals to meet the complex demands of everyday life and work in the emerging knowledge-based economy.

While these financial literacy statistics are stark, the fact remains that a compulsory system based on informed investors making rational choices fails to confront this reality.²

Data from AIST member funds says that actual member behaviour accords with the findings of behavioural economics, rather than the beliefs of doctrinaire market theorists. In fund A, 55% of all member initiated contacts came from those aged 55 and over, with a further 25% from those aged 40-54. 70% of those seeking intrafund advice were aged between 55 and 69 years. 76% of such contacts were from members with account balances over \$100,000; clearly, intrafund advice is of more value to those with higher balances.

Members closer to retirement are more likely to have actively engaged in their investments within the fund. One fund reported as follows:

Age band	0-20	21-25	26-30	31-35	36-40	41-45	46-50	51-55	56-60	61-65	66+
Default members (%)	96.1	95.9	91.8	84.7	79.7	78.2	77.8	81.0	76.4	75.8	74.8

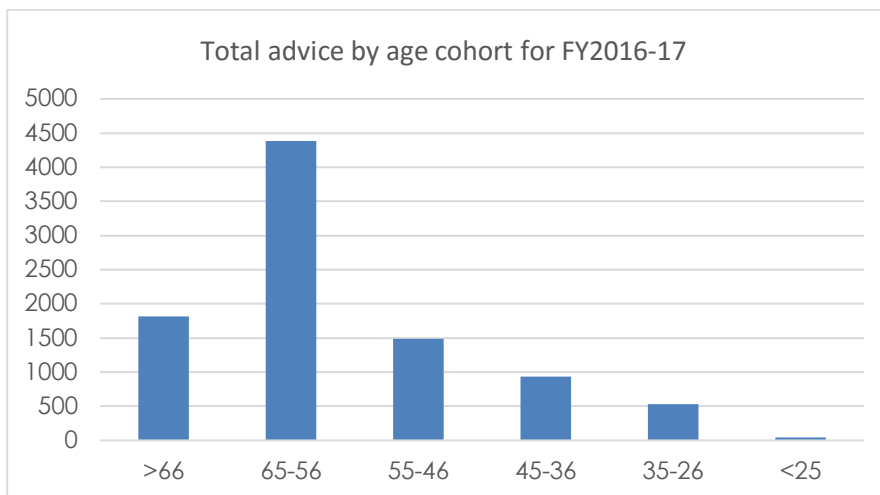
Active engagement also increased with account balance. It is noteworthy that a significant proportion of those who actively selected their investment options chose to retain some or all of their benefit in the fund's MySuper product.

² Cooper, J., Casey, K., Evans, G., Grant, S., Gruen, D., Heffron, M., Martin, I. and Wilson, B. (2010). *Super System Review final report*. Part One: Overview and Recommendations. [online] Canberra: Commonwealth of Australia, p.10. Available at: <http://tinyurl.com/zfewy9q> [Accessed 18 Aug. 2017].

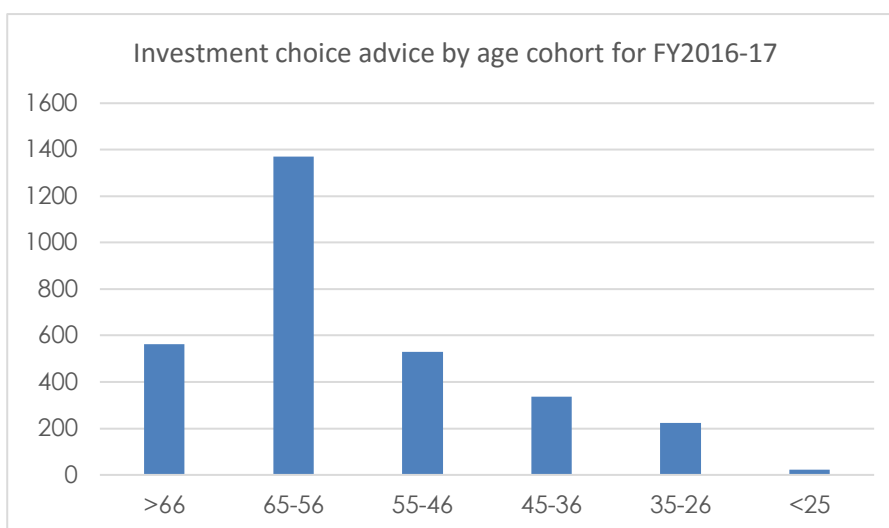
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Account balance	\$0 - 10K	\$10 - 30K	\$30 - 50K	\$50 - 100K	\$100 - 250K	\$250K+
% all ages defaulted to MySuper	90	84	80	75	71	59
% all ages chosen MySuper	7.2	9.7	11.6	14.5	17.1	23.2

In another fund, 53% of total contacts were initiated by those with account balances between \$50,000 and \$500,000, suggesting that proximity to retirement is a stronger predictor of the likelihood of making fund contact.



Advice specifically around investment options followed the same pattern.



In terms of the suitability of MySuper offerings, for the great majority of members, another very large fund reported that, of those members who exercised choice of investment strategy, 60%

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used a combination of the MySuper offering together with other options, with a skew toward higher growth. This tendency was slightly more prominent amongst members with a balance in excess of \$250,000.

Conclusion

The emphasis of the Commission, the Government and the commercial retail superannuation sector on promoting a consumer-led market is ideological, bound to lead to deadweight costs in the economy and harmful to the interests of the great majority of super fund members who are currently well served by the MySuper default arrangements – which in any event have not been given time to mature.

Unrestricted choice leading to market inefficiencies

Self-Managed Superannuation Funds (SMSFs)

As at September 2016, SMSFs held 30.3% of fund assets in direct Australian shares, 24.8% in cash and term deposits, and 15.4% in direct Australian property. Of the remaining 29.5% of the \$636 billion in total SMSF assets (as at September 2016), 14% was held in trusts (9.7% in unlisted trusts and 4.3% in listed trusts), 5% in ‘other managed investments’ and the remaining 10.5% spread across 12 other categories.”³

It is at least arguable that the collective investment profile of SMSFs represents an inefficient misallocation of capital at the national level. In particular, the heavy weighting to cash and term deposits deprives SMSF members of potential returns, while the weighting of \$97.9 billion to direct property (when combined with the government’s policy of permitting borrowings by SMSFs through limited recourse vehicles) has helped inflame the property market and reduced housing affordability for younger Australians. Thirdly, the SMSF holding of \$61.7 billion in unlisted trusts represents a clear risk to Government revenue, given the opportunity to channel trust earnings through to a super fund with a nominal tax rate of either 15% or 0%, depending on whether the member is in the accumulation or pension phase.

AIST notes economic research indicating that individual capacity to navigate complex financial decision-making declines with age. 17.7% of SMSF members were aged over 70 at 30 June 2016.⁴ The great majority of SMSFs are structured as having individual rather than corporate trustees. To

³ Power, T. (2017). SMSF investment: Three most popular asset classes, and the rest. *Super Guide*. [online] Available at: <http://tinyurl.com/yastack2> [Accessed 8 Aug. 2017].

⁴ ATO (2016). *Self-managed superannuation funds: A statistical overview 2014-2015*. [online], Table 10. Available at: <http://tinyurl.com/yacz5wnb> [Accessed 9 Aug. 2017].

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the extent that the capacity of SMSF trustees declines with age, it would be expected that either the SMSF must be liquidated and assets rolled in to an APRA regulated fund, or the economic performance of the SMSFs will decline with a consequent loss of efficiency for the sector, and further losses to the economy overall.

Excessive choice within the APRA regulated segment

APRA reported that fifteen superannuation funds – all commercial retail funds – each offered over 1000 investment options as at 30 June 2016 (excluding direct investment facilities). The maximum number of choices offered in any profit to member fund was 46; 53 commercial retail funds offered more than this.⁵

Large numbers of investment choices correlates strongly with substandard fund-level investment performance. Of the 53 for-profit funds with more than 46 investment options, only one exceeded the return of that fund over 1 year, 2 exceeded it over 5 years and none exceeded it over 10 years.⁶

It is the practice of many commercial retail trustees to place new investment offerings on their platform at the request of a particular financial planner. For those funds with very large numbers of choices, the underlying assets of many of the offerings are virtually indistinguishable. Many of them fall below the thresholds of asset size and member numbers to be reported separately to APRA. It follows that they are of little value for inter-fund competition. Excessive choice comes at a cost to efficiency, as each option must be accounted and administered separately.

Conclusion

Government policies which facilitate the offer of an unrestricted number of investment options, and which place minimal barriers for the creation of SMSFs, generate material inefficiencies within the superannuation system as a whole and, in the SMSF sector, permit material capital misallocation within the economy, add heat to the housing market and facilitate tax minimisation. And in a compulsory savings system set up to provide retirement outcomes to members, it's the members who are disadvantaged.

⁵ APRA (2017). *Annual Fund-level Superannuation Statistics*. June 2016 (Issued 1 February 2017). [online] Canberra: Australian Prudential Regulation Authority, Table 2. Available at: <https://tinyurl.com/y737gcao> [Accessed 18 Aug. 2017].

⁶ APRA (2017) as cited in a previous footnote.

Lack of appropriate data standards

AIST accepts that those members who wish to exercise choice of investment strategy, or choice of fund, should be free to do so and provided with appropriate information and tools to assist in that choice. However, despite efforts by APRA and ASIC over the past decade to improve the availability and utility of information provided by funds, the members remain poorly served in many instances.

Comparability of products is important

For both consumers and third parties, comparability of products is important. Despite the intention of MySuper enabling easy comparison between funds, this is not always the case. The inclusion of complex life cycle investment options in a simple, default product has made comparability difficult, especially where there are 5, 10 or more stages to compare. This has been compounded by variations in the types of fees, insurance offerings, declared risk appetites and strategic asset allocations.

Market analysts who compare many features of a product and then decide a rating for it have not provided a solution. Different analysts do not always compare the same features, nor do they give them the same weightings, and their ratings can be published in different and confusing ways. None of this assists members in selecting an appropriate fund.

Independent rating agencies typically focus on publishing top 10 performance tables rather than tables that include the poor performers. It is, of course, open to any fund to refuse to provide any non-public data to a ratings agency.

It is difficult, if not impossible, for a member in a long-term underperforming fund to benchmark their fund's performance. AIST recommends that APRA publish a league table showing net returns to members over 1, 3, 5 and 10 years for all MySuper products and for each Choice investment option above an agreed threshold of assets or members. This would significantly help members to identify poor performing investment options/funds over the long term.

AIST notes that the enhanced reporting measures proposed in the *Treasury Legislation Amendment (Improving Accountability and Member Outcomes in Superannuation) Bill 2017* will not address the concerns about data comparability.

This is because the measures focus on the end use of already-identified expenditure, whereas the greatest mischief in data comparability lies in the ability of some trustees to conceal or disguise payments – for example, Colonial Super Retirement Fund reports zero investment management fees. This is notwithstanding that APRA requires funds to “look through cascading entities to the first non-connected entity and reporting the ultimate asset allocation in which the investment is

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held, in addition to the investment performance of each investment vehicle which includes the associated fees, costs, taxes and other deductions”⁷.

In this respect it is noteworthy that:

- The trustee of Colonial Super Retirement Fund is a wholly owned subsidiary of the Commonwealth Bank of Australia Ltd;
- As at 30 June 2016, Colonial Super Retirement Fund reported total assets of \$4.2 billion and 179,000 member accounts and offered 590 investment options. It is not a small fund. (While the fund is not authorised to offer a MySuper product, it still reported 10% of its assets invested in a default strategy at 30 June 2016.)
- For the 2016 financial year, Colonial Super Retirement Fund reported 0.0% investment fee ratio, and 0.6% operating expenses ratio. From the perspective of disclosed fees, it looks an attractive fund for members. However, it is suffering a net outflow of both members and funds, understandable in terms of its significantly substandard investment returns.⁸

MLC Superannuation Fund, the trustee of which is a wholly owned subsidiary of National Australia Bank, also reported 0.0% investment expenses ratio and 0.0% operating expenses ratio yet generated less than median returns over 5 and 10 years.

The clear conclusion is that a fee-based selection of default superannuation funds is open to manipulation, and apparently low fee funds can produce substandard returns for members.

AIST recommends that APRA and ASIC investigate the basis on which some funds fail to accurately report the genuine costs of operating the fund, and force public correction of misleading information.

Competition through comparability is not assisted with many funds providing web-based information that is not sufficiently transparent and clear to empower consumers to make an informed decision. Low levels of financial literacy and engagement highlight the need to resolve these barriers to informed decision making.

The capacity for engaged and capable members to compare products is further limited by an array of concessions from reporting standards granted to trustees in respect of choice products.

The table in Appendix A summarises the numerous exemptions, gaps and inconsistencies afforded through the legislative environment to choice superannuation products. At 30 June 2015, choice

⁷ Reporting Standard SRS 801.0: Investments and Investment Flows

⁸ APRA (2017) as cited in a previous footnote.

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superannuation products cover \$904 billion of members' pre-retirement superannuation moneys compared with \$428 billion in MySuper.

AIST strongly recommends greater regulatory guidance on the comparability of all products to assist all parties involved in the fund selection process. This should include both default and choice products across the entire APRA-regulated sector, whether or not the fund offering the product is listed as a default fund for any employer. Default members might want to choose different investment options within their fund, or to switch funds, and both members and employers might reasonably want to understand and compare their selection/default against the wider market of superannuation funds.

Continual Changes in Government Policy

While the continual process of review of the superannuation industry since the Wallis review of 1997 has delivered efficiencies (as noted earlier), it has also resulted in an enormous and increasing compliance and regulatory change cost-burden on superannuation fund participants. It has imposed both very large direct costs on funds in responding to proposed changes, and then implementing legislated change, while at the same time distracting funds' strategic focus of boards and executives from further pursuing member interests.

In particular, AIST notes that the Government has directed the Productivity Commission to undertake this present review three years earlier than recommended by the Financial System Inquiry headed by David Murray.

Current default arrangements

Mitigating the risk of members defaulting to long-term under-performing funds

Unless trustees of all default funds engage in group think and simply seek to mirror the investment performance of their competitors, there is always going to be a risk of outperformance or underperformance, irrespective of the mechanism for identifying default funds and allocating members to them.

AIST agrees that it is highly desirable that default members be protected from the risk of being placed into long term underperforming products. We point to the 2012 requirement that members with Accrued Default Amounts (ADAs) have those amounts transitioned into a MySuper product no later than 1 July 2017 as an example of such protection being implemented through the addition of a (very basic) quality filter. As at 30 June 2016, 13 commercial retail funds still had over \$37 billion in ADAs, typically with much higher fee structures than would be permitted in a MySuper product. ADAs all derived from default arrangements between employers and the relevant commercial retail fund and, on average, lower net returns to members than provided by MySuper products.

The risk of members defaulting to long-term underperforming funds can be managed at two levels; structural and individual.

The requirements in terms of product design, fee structure and governance for MySuper reflect a structural improvement. However, AIST notes that the legislated test for authorisation is only that APRA considers the trustee “is likely to comply” with legislated minimum standards. There is no positive endorsement of the product as being good for default members. A further quality filter on products permitted to be offered as defaults, such as that to be applied by the Expert Panel of the FWC, would provide further structural safeguards.

At a consumer level, the risk of being trapped in a long-term under-performing fund could be ameliorated by providing readily accessible comparable information, and by providing regular nudges to encourage members to review their superannuation.

Current arrangements whereby employees are enrolled into each new employer’s default fund unless they choose to remain with their existing fund provides such a nudge.

The best available comparable information is the APRA data on 5 and 10 year whole of fund returns, and on MySuper returns – though the utility of the latter is reduced because of structural differences in MySuper products between single investment strategy and lifecycle models – and the practice of quoting fees as a mix of flat rate and percentage of account balance.

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AIST would support a process for the removal from modern awards of funds which substantially underperform their nominated risk and return objectives over the four year review period, and whose MySuper product provides below median net returns to members for that time.

Importantly, that process should include consideration of funds to which an employer may make contributions under an award because of grandfathering; that is, any fund to which the employer was making superannuation contributions for the benefit of its employees before 12 September 2008. Such grandfathering has provided the main means by which underperforming funds have remained available to employers as defaults – without scrutiny.

Contestability and competitive pressure

There is a widespread misconception in the community that only Profit-to-Member funds can be listed under current industrial awards. The failure by the FWC to publish a comprehensive list of all award-nominated super funds, and the awards for which they are listed, helps perpetuate that myth.

Reviewing a selection of awards demonstrates that this is not the case.

It is not difficult for funds to access the award system. For example, two funds were initially nominated under the Cemetery Industry Award in 2010, but another two were added in 2012. Under the *Hospitality Industry (General) Award 2010*, five funds were initially nominated. Additional funds were added in 2012, 2013 and 2014, while one was removed in 2014.

It can be concluded that, despite the Government's failure to give effect to the legislated enhancements to the process for identifying default funds under industrial awards, the existing award-based system is not broken. It enables funds to seek a place on the list for an assisted employer choice model, with the initial two hurdles being authorisation of a MySuper product and satisfying the FWC gateway. Funds must then compete for selection as the default at the enterprise level.

Nomination of default funds would be enhanced through implementation of the legislated additional quality filters within the FWC which are designed to ensure a MySuper product is best suited to the relevant demographic employed under the terms of a modern award. An appointed Expert Panel is to be tasked with producing a Default Superannuation List. The Expert Panel must not include a MySuper product on the default fund list unless it is satisfied that it would be in the best interest of employees that the modern awards apply to. Considerations, include, but need not be limited to:

- The appropriateness of the product's investment return target and risk profile;
- Its expected ability to deliver on the product's return target;

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- Fees and costs;
- Net returns;
- Governance practices; and
- Administrative efficiency and quality of advice.

Other relevant considerations may include insurance fees and coverage, the availability and relevance of income retirement products and member services.

The failure of the Government to appoint Expert Panel replacements and the establishment of a Productivity Commission Inquiry into the process by which default funds are allocated has delayed the introduction of the additional quality filters into the MySuper default fund allocation process.

Consumers would be better served if steps were taken to allow the additional quality filters to be applied to the default fund selection process.

Underperforming funds exiting the default market

The absence of a definitive and regularly updated list of all award nominated default funds makes it difficult to comment on changes in fund participation over time.

One success of the MySuper regime has been to encourage a number of poorly performing funds to not seek a MySuper authorisation. These funds mostly operated for profit, had mostly accessed default members via the grandfathering of arrangements that employers had in place prior to September 2008, and used the four year transition to transfer their default members into another fund operated by the same parent entity. Colonial Super Retirement Fund provides one example.

Minimising system-wide costs

Within the existing default regime, costs at the various touchpoints are generally low.

Member costs

Member search costs are close to zero, though there is no compulsion to accept a default.

Employer costs

Employer costs are low, in that (within the industrial system) they are selecting from a limited array of funds that have secured listing in relevant awards. Diligent employers would seek to compare the offerings and performance of the listed funds; this cost could be reduced if the government were to implement the legislated process for an expert panel of the FWC to provide a further quality filter on those funds listed in awards.

We are concerned the problem of direct and indirect inducements to employers to select or retain a default fund (often under the grandfathering provisions) is a clear market impediment that

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imposes costs on members. We note that this is a contentious subject where proof is often difficult to obtain. Commercial incentives and sales pressures have not been removed from the system. There is a need to examine evidence of principal-agent issues in default fund selection, including any possible direct or indirect incentives provided to employers. If a full member choice model eventuated, we would have even greater concerns about rewards for sales people, rather than members' best interests, guiding individuals into personal super accounts.

The survey work undertaken by Colmar Brunton on behalf of the ATO^{9 10} provided evidence of influence on employer superannuation decision making, including the provision of incentives. The concern is not that banks offer superannuation products to individuals, but where banks offer packaged services to employers that involve business banking and default superannuation services to employees of the business.

A key sales point to employers is the perceived advantage to the employer of a one-stop service. There is no legislative prohibition on an employer choosing a retail superannuation fund as their default fund solely because it is more convenient for the business. This convenience does not benefit the member of the fund chosen by the relevant employer; in fact, the evidence is where retail funds associated with banks are chosen by employers, the net returns to members of the relevant default funds are on average less and significantly less over time.

It is also suggested that whilst the offer of an inducement, say a discount of business banking rates, by the trustees of a fund is prohibited, it is not necessarily a contravention of s68A of the SIS Act for an employer to benefit from reduced rates that apply to bundled services. In fact it is suggested that it is common practice amongst banks for interest rate and other discounts and benefits to be increased where the business relationship is larger. In such circumstances, there is a clear incentive for an employer to include employee default superannuation arrangements in the transaction.

While AIST supports employers being involved in the default selection process (as they are currently) this is only appropriate where there is a heavy filter and regulation to prevent inappropriate behaviours such as inducements, soft third-line forcing, and other inappropriate

⁹ Colmar Brunton, (2010). *Investigating Superannuation: Quantitative Investigation with Employers*. Final Quantitative Report prepared for Australian Taxation Office. [online] Canberra: Australian Taxation Office, pp.55-57. Available at: <http://tinyurl.com/m9go3ww> [Accessed 26 Oct. 2016].

¹⁰ Colmar Brunton, (2010a). *Understanding Superannuation Preliminary Report: Qualitative Investigation with Employers, Consumers & Industry*. Prepared for Australian Taxation Office 25 March 2010. [online] Canberra: Australian Taxation Office, p.28. Available at: <http://tinyurl.com/hxto3jv> [Accessed 26 Oct. 2016].

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cross-selling. The inherent conflict of interest in an employer recommending a default fund from a provider from which it receives other financial services is well recognised by the general public. An AIST-commissioned Essential Media poll conducted earlier this year found that almost three out of four respondents agreed that an employer shouldn't be able to select a default fund that is associated with their bank.

AIST recommends that the Commission prohibit an employer from choosing, as its default fund, a superannuation fund that is part of a financial institution from which it receives other financial services. We also recommend that the Commission continue to explore the benefits of extending fiduciary responsibilities to employers in Australia.

Fund costs

Fund costs are medium, in that they must meet standards for a MySuper product, must engage with relevant employers if they wish to be nominated as the default fund at an enterprise level, must seek to design their MySuper product for the particular demographic the fund is targeting, and must engage with the industrial system in order to be nominated under relevant modern awards. Furthermore, through industry levies, funds (and hence members) pay the full costs of regulation other than through the industrial framework.

Costs to Government

Costs to government are very low, unless systemic underperformance of MySuper products and/or a failure in government policy settings around the interaction of the superannuation, tax and social security systems means that age pension outlays are higher than they would be in a well-managed and well-regulated system. Implementation of the legislated additional quality filter through the expert panel of the FWC would help to further mitigate these risks.

Maximising long-term net returns and allocating members to products that meet their needs

The alignment of funds with particular industries through the award-based determination of default funds provides the opportunity for a deeper and more predictable knowledge of the member base in order to design MySuper, other choice investment options and insurance offerings tailored to the needs of the funds' demographic.

For example, AIST member funds have reported that they considered risk preferences of members, likely retirement outcomes, work patterns, level of income (based on Superannuation Guarantee paid), other investment assets, potential age pension reliance, and recovery from investment market shocks versus alternative lower risk or de-risking lifecycle approaches. The success of that approach is clear, with one fund reporting 93% of members having some or all of their benefit in the MySuper product, including some members who have been identified as

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changing investment strategy at one point and then reverting to being fully invested in MySuper. Of those who have exercised choice, more move to a higher risk and return strategy than to lower.

At the same time that they can tailor product to members drawn from a particular industry, some funds can use their industry knowledge to identify investment opportunities which simultaneously provide strong returns for relatively low risk, as well as providing employment opportunities for their members. Cbus is well recognised in this regard.

Profit-to-Member funds stand out for securing insurance arrangements that are highly beneficial for members, and especially those who may ordinarily experience difficulty in obtaining insurance.

For example, in industries with a higher proportion of casual employees and/or sole traders who do not benefit from employment-based sick leave, income protection insurance is provided either as a default, or as a default for recognised segments of the fund membership unlikely to have sick leave provided.

Industry or enterprise based funds also report that, using a combination of scale and specific sector knowledge, they can work with their insurers to ensure coverage for high risk occupations at acceptable pricing, and to work with members' employers to manage risk. For example, one fund had experienced a worsening claims experience from one of its insurance categories, whereby there would have been adverse impacts on members' retirement outcome. However, through an agreement with the relevant employer, it could provide appropriate coverage level at an affordable price while taking into consideration the specific needs of the membership cohort.

Impact of current default arrangements on stability in the superannuation system that could lead to significant systemic risks

AIST does not consider that current default arrangements provide any concern about industry stability, nor generate systemic risk.

Any material disruption to existing arrangements that led to the large scale transfer of members between funds would generate excess volatility in Australian investment markets and could cause harm to the real economy as well as to members' retirement savings.

Greater systemic risks lie in the concentration of service providers to the industry, especially in terms of custody and fund administration. AIST generally considers that the identification and management of systemic risks needs to take place at a prudential level.

Transition to a New Default Allocation Mechanism

Each model proposed by the Productivity Commission anticipates fewer default funds, generally between 4 and 10. This means that 92-97% of existing default funds (i.e., funds that provide a MySuper offering) would lose their default status. Whatever the transition arrangements, this would result in many funds becoming cash flow negative, would disrupt efficient business models, and require a restructuring of asset allocations and investment strategies. The flow on effects to the economy, fund members and investment returns could be large and negative, leading to stranded products and members, potentially increasing the cost of the Age Pension over time.

We are not aware of research which quantifies the costs to members, funds, Government or others in relation to such a transition. It would be very clearly bad policy to make recommendations in relation to this without such costing being undertaken.

AIST considers that the Productivity Commission has undertaken this review with a preconception about changing to a different mechanism for deciding default funds, without proper consideration of the existing system or the improved, legislated but untried system.

AIST rejects that approach as not sufficiently impartial for a statutory body required to give independent advice to government.

Constitution of a body for selecting default funds

AIST rejects the surprising stance of the Productivity Commission that judicial arrangements are not subject to accountability¹¹. This unsupported view greatly reduces the value of the inquiry, and damages perceptions of the Commission as an independent body.

For the record, AIST notes extensive layers of accountability surrounding judicial processes in Australia, including but not limited to the capacity for aggrieved persons to appeal a judicial decision, the requirements for judicial officers to hold hearings in public and give reasons for decisions (and so be subject to public and political scrutiny, even as they maintain judicial independence), and the legislated capacity in many jurisdictions for judges to be removed for incompetence or misconduct. For further commentary, see Kirby, 2001¹².

AIST supports the selection of default funds by a government body that has the characteristics identified by the Commission in its second draft report. However, we do not support the creation of a new body for this purpose, noting that such a body already exists to administer the selection of defaults. To create a new one is cumbersome, bureaucratic and increases the risk of politicisation, but is highly unlikely to have the judicial and legislative controls that regulate the FWC.

The suggestion that the panel determining eligibility for preferred default status would meet only for the period it was required and then cease operations appears to be absolutely inconsistent with accountability, and does not lend itself to the building of the requisite expertise.

AIST strongly considers that the body should have sufficient expertise to evaluate potential default products.

We note that members of an expert panel of the FWC are appointed by the relevant Minister on recommendation of an independent, merit-based selection process conducted by senior representatives of the Commonwealth Department of Employment and the Australian Public Service Commission, in consultation with the Shadow Minister for Workplace Relations and the States and Territories.

¹¹ PC (2017). *Superannuation: Assessing Competitiveness and Efficiency*. Productivity Commission Issues Paper, July 2017. [online] Canberra: Productivity Commission, p.22. Available at: <http://tinyurl.com/ydzd8a7a> [Accessed 21 Aug. 2017].

¹² Kirby, M. (2001). *Judicial Accountability in Australia*, [lecture]. Commonwealth Legal Education Association, 6 October 2001, Brisbane. [online] Sydney: The Hon Justice Michael Kirby AC CMG. Available at: <https://tinyurl.com/y7ejgzmf> [Accessed 18 Aug. 2017].

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Whatever individuals make up a body to apply a quality filter will bring their own experiences and value systems to the process. The combination of an independent merit-based process together with the engagement of the relevant Commonwealth Minister, shadow Minister and the States clearly mitigates the risk of politicisation and bias.

In terms of access to the selection process, AIST notes that there is no evidence of super funds that have sought to be considered for inclusion in a default fund listing under current arrangements being excluded from fair consideration. It has been open for any fund to seek the support for listing from either an employer or employee representative, and it is noted that some (but not many) retail funds have done this.

AIST therefore strongly endorses the existing legislated arrangements for a quality filter of default superannuation funds to be applied by an expert panel of the FWC.

Estimating the utilisation and pass through of economies of scale

Estimations of unrealised scale benefits are important in assessing overall industry structure.

We note that the Commission's focus in this segment is purely on institutional funds. We believe the Commission should also consider whether high costs per member for SMSFs represent a drag on performance of the industry overall.

If the view is taken that materially higher absolute costs in the SMSF sector are acceptable when the members' choice to establish the fund is taken into account, then this should at least be made explicit.

While the currently legislated scale test applies only to MySuper products, not at the fund level or for other products, AIST welcomes APRA's proposal to extend the requirement for quality assessments across all products.

Excessive choice of investment strategy increases costs for funds overall with a severe lack of scale in the great majority of options - driven by adviser preference. Note that funds are required to provide data to APRA only in respect of options that "at the most recent 30 June has assets relating to non MySuper interests which represent more than 5% of the total assets of the RSE or has assets greater than \$200 million or which underlies a defined benefit pension or interest"; that is, the least economic options are explicitly excluded from reporting requirements so information about them is not readily available.

Average assets within each option not individually reported can be inferred by calculating, for any fund, $(\text{total fund assets} - (\text{assets in pension phase} + \text{MySuper assets} + \text{assets reported in form 601.0 item 6 - reserves})) / (\text{total number of investment options} - \text{number of options reported at form 601.0 item 6})$. While at an individual and fund level it can be argued that diseconomies at this level don't matter so long as the member is happy to pay and costs are quarantined from other fund members (which must be problematic), at a system level it is clearly inefficient, especially as many of the multiplicity of options are readily substitutable.

Investment performance benchmarking

Care would need to be taken to measure returns net of both fees and tax, and to have regard to survivor bias when comparing funds' achieved returns by asset class against asset-based benchmarks like indices.

AIST challenges the Productivity Commission proposal to assess only default products across market segments (which it defines as SMSFs, institutional funds, accumulation and retirement segments).

Firstly, even on its own terms the Productivity Commission needs to be clear that "default" includes the default investment options within master trusts, not just the default option within default funds named in industrial awards and agreements.

Secondly, when assessing system level outcomes, the efficiency of the aggregate of choices made by individuals should be incorporated into the assessment. This is unlikely to be possible at product level, but demands that whole of fund returns be examined. In particular, if the aggregate of member choice (both within the institutional sector and for SMSFs) generates sub-optimal returns, that requires focus on each of:

- Members' capacities to make choices;
- The role of trustees in putting various choice options on their menus; and, especially,
- The role of advisers in influencing strategic asset allocations.

It is also inappropriate for the Productivity Commission to consider "institutional" funds as a whole, given the demonstrable difference in outcomes achieved by Profit-to-Member and commercial retail funds. There is unlikely to be sufficient longitudinal data for a realistic discussion of retirement products under this criterion, with most coming from AMP and Challenger, with some funded DB pension schemes also being available but having quite different characteristics from the annuity and developing account-based pension elements.

Potential ‘foundation’ reforms

The establishment of a centralised online service for members, employers and Government, building on the existing functionality of myGov and Single Touch Payroll

AIST supports the further development of myGov and Single Touch Payroll to make it easier for members and employers to keep track of their superannuation transactions.

A centralised clearing house administered by the ATO

AIST endorses the previous submission of the Gateway Network Governance Body Ltd that the objectives intended by a single, centralised clearing house are currently being met effectively and efficiently by the implementation of SuperStream and the operation of the Superannuation Transaction Network.

AIST notes that SuperStream has involved the legislative and actual implementation of a contributions pass-through requirement. This means that if a superannuation fund offers a MySuper product, then that superannuation fund is required to pass on contributions data it receives from any of its default employers relating to any other superannuation funds. This is another initiative that can simplify the administration of superannuation for employers, and means that an employer need only ever send their superannuation contributions to one super fund.

While we have no discomfort with government providing services where there is a failure in the commercial market, or where government can provide services more efficiently and effectively, we do not consider that the case has been made out in this instance for changing from an effective commercial arrangement with a number of participants to a nationalised model.

Particularly in light of systems reliability issues experienced by the ATO over the past two years, AIST considers that moving from the current effective distributed network of gateway providers, with the inherent advantage of systems redundancy, would introduce an unnecessary degree of systemic risk.

Proposed merger transparency framework

AIST welcomes APRA’s release of SPG 227 Successor Fund Transfers. This guidance provides clarity around the operation of the ‘equivalence’ test in a way that should facilitate future merger activity from the perspectives of both exiting and receiving funds.

Similarly, the creation of an “outcomes” test applying to trustees in respect of both MySuper and choice products should provide further impetus towards mergers or takeovers – as well as

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requiring trustees to provide greater justification of excess levels of choice of investment strategy within funds.

AIST considers it reasonable for funds to be required to advise APRA within 14 days of merger explorations which proceed to the point of a formal request from one party to another to have access to data to conduct due diligence in respect of a merger. AIST would have no objection to funds being required to advise members by way of the annual report in respect of merger proposals which had been commenced but not proceeded with. There should not be a requirement to disclose merger proposals to members where the outcome had not yet been determined, as that could of itself impact the merger discussions.

Introduction of a first timer default mechanism.

As noted in our submission in response to the Productivity Commission draft report of April 2017, AIST understands that account proliferation is a primary driver for the Commission's preference for members to be allocated to a default fund only when they first join the workforce. That issue is in the process of being resolved through the combination of legislative and technological change embodied in SuperStream and Single Touch Payroll.

AIST is deeply concerned that requiring first time employees to select a fund that they may stay with for life risks creating a wide scope for mis-selling, even when the available products have been pre-qualified. The highest vulnerability lies in young people, once recruited into a fund, being induced to shift from a quality-assessed MySuper product into a suboptimal Choice product.

Young people joining the labour market for the first time are furthest from retirement, and typically have the least interest and knowledge about superannuation or other financial matters relating to retirement. They are also more likely to make decisions or allow decisions to be made on their behalf on the basis of short-term considerations, even short-term inducements. Even with the ever-present option of choice, a default system whereby a fund is allocated for life is likely to lead to a lowest common denominator marketing campaign, focused on aspects other than maximising retirement income.

By contrast, older members – those entering middle age and beyond – have a greater appreciation of the reality of retirement. They have much higher interest and knowledge about superannuation, particularly as their fund balances increase, and are less likely to be distracted by short term inducements.

Milestone events such as health issues, change in employment and relationship status should all give prompts to review retirement readiness, and it is counter-intuitive to suggest that one of these prompts (consideration of superannuation at change of job) should be removed.

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The additional protections which apply to MySuper members may result in these members being regarded as a burden to a trustee with a duty to generate profits for shareholders. Once an employee has joined a fund, they are vulnerable to being encouraged into Choice products which are likely to generate higher profitability for the fund, even though that may not be in the interest of the member. This is particularly the case when sales staff who are not engaged by the trustee have regular interactions with the member and can raise superannuation-related matters in the context of a broader conversation about the person's financial arrangements.

Appendix A: Overview of exemptions from regulatory framework

Different treatment	Comments	Impact on consumers
<p>No explicit duties on trustees to promote the financial interests of beneficiaries, or apply a scale test for choice products/investment options.</p>	<p>The value of retirement savings in pre-retirement choice products /investment options is double the value in MySuper products.</p> <p>In 2014 SuperRatings found substantial differences between fees for MySuper and choice products, particularly within retail superannuation funds – even when the underlying asset allocations were almost identical.</p> <p>According to APRA there are 120 MySuper products but over 40,000 member investment choices.</p>	<p>The compounding effect of higher fees over long term reduces retirement incomes for members of choice products.</p> <p>Choice overload baffles members.</p> <p>The choice sector of the superannuation system is not achieving efficiencies of scale.</p>
<p>The Government deferred the requirement for choice dashboards in 2014, 2015 and 2016.</p> <p>It plans to amend the law so funds would only need to produce dashboards for their 10 largest choice options.</p>	<p>The Super System Review, Financial System Inquiry, and the Grattan Institute have all concluded that the level of fees paid by members is too high.</p> <p>SuperRatings has criticised the poor level of disclosure of fees, noting there is still a long way to go to achieve comparability of fees across MySuper and choice products/investment options.</p>	<p>Members of choice products/investment options do not have a dashboard and so cannot easily compare their returns, fees or costs with MySuper products.</p> <p>Under the Government’s proposal, dashboards will not be required for most choice investment options.</p>
<p>APRA does not collect or publish statistics on choice products/investment options equivalent to the comprehensive statistical collection derived from the MySuper reporting standards.</p>	<p>APRA deferred collecting data for choice products/investment options for consideration during the development of the requirements for choice dashboards.</p>	<p>Members rely on APRA, employers, advisers, Government, researchers, commentators and trustees to analyse the characteristics and performance of choice products/investment options. Lack of data hampers this.</p>
<p>No requirement to ensure switching funds is in the best interests of the member when giving general advice or under</p>	<p>ISA analysis of Roy Morgan research found an increase in cross-selling retail superannuation using general advice and no-advice business models.</p>	<p>Members are switched from a MySuper product to an inferior choice product/investment option, when it is not in the best interests of the member.</p>

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Different treatment	Comments	Impact on consumers
no-advice business models.		
New fees and costs disclosure requirements do not apply to superannuation held via a platform.	<p>According to Rainmaker, over 70 per cent of retail superannuation assets in Australia are held via platforms.</p> <p>According to Lane Clark Peacock, UK members may be paying up to 20 basis points per annum to access an active fund through a platform when compared with the cost of going direct to the fund manager.</p> <p>According to the UK Financial Conduct Authority, platforms add 20-90 basis points to costs.</p>	<p>Disclosure for superannuation held via a platform understates fees and costs paid by the member.</p> <p>ASIC admits it would be misleading to compare the fees and costs of platforms and non-platform superannuation funds.</p> <p>The compounding effect of higher costs over long term reduces retirement incomes for members.</p>
The (unimplemented) dashboard regime for choice products/investment options will not include platforms.	While the Government amended the regime to require dashboards for products/investments held via a platform, platforms themselves will be exempt.	Members who hold their superannuation via a platform will not have a dashboard for it, compounding an existing difficulty comparing their returns, fees or costs with MySuper products.
APRA does not collect or publish statistics on platforms equivalent to the comprehensive statistical collection derived from the MySuper reporting standards.	APRA deferred collecting data for choice products/investment options for consideration during the development of the requirements for choice dashboards.	Members rely on APRA, employers, advisers, Government, researchers, commentators and trustees to analyse the characteristics and performance of superannuation held via a platform. Lack of data hampers this.
No requirement to produce a shorter PDS for legacy products.	According to Rice Warner, around 30% of personal superannuation assets are held in legacy products.	This makes it difficult for members in legacy products to compare the performance, fees or costs of the product with a contemporary product, understand the exit costs and assess whether they would be better off switching to a contemporary product.
The (unimplemented) dashboard regime for choice products/investment	Rice Warner found fees and costs for legacy products are on average more than double those for contemporary products.	Members who hold legacy superannuation products will not have a dashboard, making it difficult to



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Different treatment	Comments	Impact on consumers
options will not include legacy products.	UK Independent Project Board found £26 billion in legacy pension schemes had investment manager fees above 1%, with nearly £1 billion exposed to fees over 300 basis points per annum.	compare their returns, fees or costs with contemporary products.
APRA does not collect or publish statistics on legacy products equivalent to the comprehensive statistical collection derived from the MySuper reporting standards.	APRA deferred collecting data for choice products/investment options for consideration during the development of the requirements for choice dashboards.	Members rely on APRA, employers, advisers, Government, researchers, commentators and trustees to analyse the characteristics and performance of legacy products. Lack of data hampers this.
Conflicted remuneration is banned for most of the financial services industry, but there is an exemption for advice about retail life insurance.	In 2014 ASIC found more than one third of advice about retail life insurance reviewed did not comply with the law. 96% of non-compliant advice was given by advisers paid an upfront commission.	Consumers are at significant risk of being recommended a life insurance policy that is not in their best interests. Industry and Government proposals to address this do not include banning commissions.



Appendix B: AIST response to Productivity Commission's intended criteria and indicators for assessing competitiveness and efficiency of the superannuation system



Issues paper criteria	PC - indicators within each assessment criteria	PC proposed way to measure and assess	AIST summary indicator	AIST comment
C1. Is there informed member engagement?	Financial literacy of members compared to an 'adequate' standard (input)	C1: PC proposes using member surveys, fund disclosures and case studies to provide evidence.		AIST agrees that informed member engagement is theoretically desirable but believes that there is ample evidence that financial literacy is low across large subsets of the population and is not improving (e.g. ANZ 3 yearly survey). AIST has very significant reservations about PC methodology in conducting member surveys for its Stage 2 draft report, and failure to consult on content or methodology for proposed survey addressing this issue. Behavioural economics says education and disclosure are not the answers to market weakness when consumer capacity is low, costs are immediate and any benefits are remote.
C1. Is there informed member engagement?	Member superannuation and insurance literacy#* (input)	C1: PC proposes using member surveys, fund disclosures and case studies to provide evidence.		Note ANZ survey doesn't address insurance through super so that will need to be specifically addressed



<p>C1. Is there informed member engagement?</p>	<p>Member active account activity: voluntary contributions and uptake of intrafund advice</p>	<p>C1: PC proposes using member surveys, fund disclosures and case studies to provide evidence.</p>		<p>Voluntary contributions are restricted to those with spare savings capacity. APRA data shows numbers of members with MySuper interests as a result of investment choice; that should be a clear indicator of informed engagement.</p>
<p>C1. Is there informed member engagement?</p>	<p>Changes to investment/ insurance options* (input, behaviour)</p>	<p>C1: PC proposes using member surveys, fund disclosures and case studies to provide evidence.</p>		<p>Reliability of survey data is likely to be higher in relation to switches than other aspects the PC is considering. AIST notes that trustees that get their defaults right from a member perspective will find a low incidence of switching even from engaged members. An increase in switching rate, either between and within default and choice funds or between institutional funds and SMSFs can be impacted by factors other than competition. In general the level of switching between investment choices can fluctuate according to volatility of investment markets. According to a report by Paul Gerrans for AIST, during the period of the GFC five to seven per cent of members made an investment switch, with the majority of these members having made just the one change to their investment strategy, and with 20% making more than one switch. Members who made one switch only may have crystallised losses permanently if they moved to cash and did not take advantage of the rebound over the following three years. In terms of the indicator it would be important to be able to understand the impact of investment markets on switching behaviour. An interpretation that a higher switching rate is a positive indicator is likely to be inaccurate and misleading.</p>




<p>C1. Is there informed member engagement?</p>	<p>Member account monitoring activity: use of fund websites; use of online calculators; call centre enquiries* (input, behaviour)</p>	<p>Member surveys; fund disclosures; case studies</p>		<p>Data is likely to be weak, especially with regard to channel. Member surveys highly unreliable, fund disclosures variable and highly aggregated where available, case studies selective. A selection of AIST member funds report between 4.8% and 10% member contacts in a month. Members with balances between \$100,000 and \$250,000 were by far the most likely to contact the fund; i.e. engagement increases with account balance. One fund reported that claims, pensions and inward rollovers were the most common reasons for contact.</p>
<p>C1. Is there informed member engagement?</p>	<p>Use of advisers by members and/or member intermediaries (input)</p>	<p>Member survey</p>		<p>We do not agree that this is an indicator of members making informed decisions, as this could be an inverse measure of information asymmetries and/or of the use of "advisers" as a sales channel. An efficiency measure for the superannuation system is the extent to which an individual super fund member is able to access the full range of features of superannuation with minimal need for financial advice: Over the long term a measure of efficiency could be the use of online information such as calculators and robo-advice tools which will become more sophisticated. In the short term the use of financial advisers may be influenced due to demographics and the regulatory complexity of Centrelink and superannuation interactions. In particular, the baby-boomer generation is larger than following generations and may result in short term demand for financial advice as baby boomers transition to retirement. AIST believes that an efficient superannuation system is one which minimises the need for expensive financial advice.</p>



<p>C1. Is there informed member engagement?</p>	<p>Fund expenditure on member education and engagement as a proportion of total marketing expenditure* (input)</p>	<p>Research firms; fund disclosures; fund surveys</p>		<p>AIST considers this is an ambiguous indicator that depends on the definition of expenditure on member education and engagement, as well as on marketing. It is likely to be difficult to disaggregate data that is specifically targeted for member retention. We also note that it will be difficult to separately identify expenditure on “group” or brand advertising (e.g., in a multiple product financial conglomerate) from product or single super fund marketing expenditure. We are also uncertain what constitutes a “bad” score for this indicator. Is it a high spend? Member retention is needed as proof of competitiveness, as well as scale.</p>
<p>C1. Is there informed member engagement?</p>	<p>Availability of meaningful and comparable information on fees, product features (including insurance) and risks#* (input)</p>	<p>Reviews by others; member surveys</p>		<p>AIST endorses this indicator but cautions that member perception of availability of information is likely to be skewed by engagement. Thus not level playing field. Critical that member surveys stratify by characteristics such as age, gender, NESB, income and account balance. Of course, everyone conforms to PDS requirements, but the fact that most don't read those in detail if at all demonstrates how difficult this issue is. Further, difficulty in gaining agreement on RG97 demonstrates fractured industry views.</p>
<p>C1. Is there informed member engagement?</p>	<p>Fund and product switching costs for members (administrative, search and learning costs) and costs to opt out of insurance (input)</p>	<p>Member surveys; research firms</p>		<p>The absence of such costs should be a positive indicator, but AIST cautions that administrative fees are likely to be gamed. As SuperStream reforms are bedded down transaction costs should reduce. Learning and search costs are still very high given current disclosure regimes, especially in the Choice environment.</p>



<p>C2. Are active members and member intermediaries able to exert material competitive pressure?</p>	<p>Defined contribution members that do not have choice of fund (input)</p>	<p>Regulator data</p>		<p>AIST notes that this indicator was not included in the Commission's first draft report, so there has been no prior opportunity for comment. The implication of the question is that the PC seeks to support its narrative that the industry is uncompetitive and action should be taken to engender competition, especially in the default space. AIST notes that enterprise agreements that specify a single superannuation fund for employees generally provide for enhanced super benefits for those employees.</p>
<p>C2. Are active members and member intermediaries able to exert material competitive pressure?</p>	<p>Size of the SMSF sector (funds and members) relative to institutional sector (output)</p>	<p>Regulator data</p>		<p>Over time there are a number of factors that may influence the growth of the SMSF sector, including legislative and tax settings, permissible leverage, and the significant influence of advisers. A long term structural issue that SMSF trustees must manage is cognitive decline. It can be expected that, over the long term that as the population of SMSF trustees age, where an individual trustee suffers cognitive decline they close their SMSF on the basis of the inability to exercise trustee duties adequately. We point out that SMSFs are rarely set up without advice and that the reliance on intermediaries and the capture of the aging trustee is a barrier to exit which could lead to an inefficient growth in SMSFs.</p>



<p>C2. Are active members and member intermediaries able to exert material competitive pressure?</p>	<p>Changes in market shares of funds (output)</p>	<p>Regulator data</p>		<p>AIST agrees with this indicator and proposes its expansion to consider the different value propositions of the different sectors. It can be expected that in the long term that super funds or sectors that deliver better performance will increase their market share, depending on other factors such as marketing, advertising and distribution spend.</p>
<p>C2. Are active members and member intermediaries able to exert material competitive pressure?</p>	<p>Switching rate between and within default and choice products and between institutional funds and SMSFs (behaviour)</p>	<p>Member surveys; fund surveys; research firms</p>		<p>There is confusion on the part of the PC between default and choice funds and default and choice products. There is of course no capacity to switch within a default product. Members can choose to switch from a default product to one or more other investment options (choice products) within the same fund, or switch to a default or choice investment option within another institutional fund, or to an SMSF. An increase in switching rate, either between and within default and choice funds or between institutional funds and SMSFs can be impacted by factors other than competition; for example 5-7% of members switched investment strategy during the GFC, often to their detriment.</p>




<p>C2. Are active members and member intermediaries able to exert material competitive pressure?</p>	<p>Default rates for funds, accumulation products and insurance (behaviour)</p>	<p>Regulator data; member surveys</p>		<p>If there is use to be made of this information, it should include data on members in default and choice products within master trust sub-plans. Consistent demand for default fund products is not an indicator of a lack of competition, but an indicator that the default funds are meeting long term needs and preferences of members. The establishment of MySuper means that the overall quality of default fund products across the system has improved. Members in default fund investment options, may have actively chosen their option - demonstrably so in some cases where they hold both MySuper and choice interests within the same account.</p>
<p>C2. Are active members and member intermediaries able to exert material competitive pressure?</p>	<p>Fee dispersion* (output)</p>	<p>Research firms; fund disclosures</p>		<p>This is a sound indicator of competition at the industry level; in a fully functional customer driven market, there would be little fee dispersion. Weakness is in the definition of fees, as discussed elsewhere. A greater dispersion between default and choice products does not necessarily indicate that a member is receiving enhanced services but may be an indication that a member is unaware of the impact of costs having been sold a product via a financial adviser. Dispersion could therefore be an indicator that providers are seeking to “game” the default fund selection system by churning members of default funds into higher fee products. In any event, the consideration of fees in isolation to net returns is concerning as it should not matter how products make their returns, just that they should be good after fees are taken into account.</p>



<p>C2. Are active members and member intermediaries able to exert material competitive pressure?</p>	<p>Corporate fee discounts (output)</p>	<p>Regulator data</p>		<p>The presence of fee discounts indicates a competitive market between the banks as suppliers of superannuation services, and employers as suppliers of significant numbers of members/assets which will generate profit to the bank. AIST has no objection to this practice so long as the discounts benefit members and there is no subsequent churn of MySuper members into higher cost choice products.</p>
<p>C3. Is the market structure conducive to rivalry?</p>	<p>Market concentration at wholesale and retail levels (Herfindahl-Hirschman Index and market shares of largest providers)* (output)</p>	<p>Regulator data</p>		<p>Agree with this indicator, although we think it is likely to be of limited use in the super funds sector of the system. The collective market share of the largest firms in the industry is likely to increase in the short term through industry consolidation. In the long term it is desirable that there is a diversity of providers. The HHI will be more relevant in measuring concentration in custody and administration services where the systemic risk is likely to be concentrated though it is unlikely that data will be available in respect of them.</p>
<p>C3. Is the market structure conducive to rivalry?</p>	<p>Number of institutional funds (input)</p>	<p>Regulator data</p>		<p>Agree with this indicator. In the short term there is the potential for industry consolidation. In the longer term it is desirable that there is a diversity of providers.</p>


<p>C3. Is the market structure conducive to rivalry?</p>	<p>Height of barriers to entry — effect of default rules on market entry (input)</p>	<p>Fund surveys; case studies; reviews by others</p>		<p>If the issue is barriers to entry for creating an RSE licensee, the answer is "very low" in terms of regulatory barriers. Market barriers are much higher, and relate to the establishment of a distribution mechanism and getting people to sign up for a complex long term financial product from an entity without a track record. Regulatory barriers to creation of a MySuper product are a modest but important protective element to the system which has been specifically designed to provide protection for those who do not choose a fund.</p>
<p>C3. Is the market structure conducive to rivalry?</p>	<p>Height of barriers to entry — market impediments to funds accessing distribution channels (input)</p>	<p>PC proposes using fund surveys; case studies; reviews by others</p>		<p>Depends on definition of market and is different for different market segments. Key is accessing flow of contributions in order to build a stock of FUM. Very significant non-regulatory barriers in terms of distribution channels - typically accountants for SMSF providers, bank branches/relationships with employers, and financial planners for commercial retail funds and industrial system for P2M. Noteworthy that commercial retail funds can demonstrably access the default segment through the industrial award system while access to "commercial" channels is very rare for P2M funds. Data on control over distribution mechanisms is not easy to obtain.</p>

<p>C4. Is the market contestable at the retail level?</p>		<p>Entries, exits and consolidations of funds# (behaviour)</p>		<p>Except in relation to MySuper products, proposed data will not reveal internal fund consolidation. Particularly for retail sector, maintenance of excessive numbers of sub-plans and choice products is a significant source of complexity and inefficiency. Legacy sub-plan structures are a genuine issue for commercial retail funds but quite opaque. Severe agency risk if accountants etc take over as personal legal representative of SMSF trustees as they age. APRA's release of SPG 227 is welcome as removing an inhibition to funds undertaking successor fund transfers, although the final version is a bit less facilitative than was the draft. Overall data on industry structure is easy to obtain, reliable and useful.</p>
<p>C4. Is the market contestable at the retail level?</p>	<p>Proportion of administration and investment services provided in-house, outsourced to related parties and outsourced to unrelated parties (input)</p>	<p>PC proposes to use Regulator data; fund disclosures; fund surveys</p>		<p>Consistency and transparency are potential issues due to definitions of "related parties".</p>

<p>C4. Is the market contestable at the retail level?</p>	<p>Proportion of insurance services outsourced to related parties (input)</p>	<p>PC proposes to use Regulator data; fund disclosures; fund surveys</p>		<p>Colonial First State investment is through a single life policy with CommInsure. What happens after the money reaches CommInsure is generally not transparent. APRA requires look through to the first non-associated entity level for the purpose of reporting asset allocation, but does not currently collect look through reporting on management fees. Thus a key detriment of vertical integration - the capacity to use layers of multiple party transactions to generate fee income - is not transparent, while allowing the fund to report competitive headline fees. That is a fundamental reason why the only genuine comparator is risk-adjusted returns to members, net of tax and all fees. Note that in the case of Colonial First State, investment management fees are reported as zero. With regard to risk insurance, a better indicator of the impact of related party service provision would be price/member of comparable products, the incidence of individual underwriting required by related party insurers and the ratio of premiums to payouts over a lengthy (say 10 year) period for similar insurance products when provided by related and unrelated insurers.</p>
<p>C4. Is the market contestable at the retail level?</p>	<p>Switching between insourcing and outsourcing of wholesale functions by funds (behaviour)</p>	<p>PC proposes using fund disclosures; fund survey</p>		<p>Very limited indicator as only very large funds have the capacity to choose between insourcing and outsourcing functions.</p>

<p>C4. Is the market contestable at the retail level?</p>	<p>Alignment in the structure of member fees and underlying costs#* (output)</p>	<p>Regulator data; fund disclosures; research firms</p>		<p>Not transparent. Member fees can be manipulated in a vertically integrated group by covering costs and generating profit in downstream related parties.</p>
<p>C5. Are there material anticompetitive effects of vertical and horizontal integration?</p>	<p>Cost and member fee differences from outsourcing services to related versus unrelated parties (output)</p>	<p>Fund surveys; regulator data; fund disclosures</p>		<p>Agree with this indicator. We have interpreted this indicator to mean that the best case outcome is that a related party outsourced provider results in reduced costs and a negative outcome would be increased costs arising from using related party outsource providers.</p>
<p>C5. Are there material anticompetitive effects of vertical and horizontal integration?</p>	<p>Transparency and efficacy of fee disclosure by funds, including for distinct services# (behaviour)</p>	<p>PC proposes to use reviews by others</p>		<p>Data is difficult to identify, but this indicator is important to assist in developing transparency and a level playing field. Note again the 0% reported investment management expenses from CFS -demonstrating the risks of a fee based competition for default fund status. We note further legislative support is required for system wide disclosure and that there are current challenges with implementation of RG97.</p>

<p>C6. Do funds compete on costs/price?</p>	<p>Costs relative to assets and number of accounts by service (investment, administration and insurance services) and by market segment (input)</p>	<p>PC proposes using Regulator data; research firms; fund disclosures.</p>		<p>Costs tend to be opaque, especially in relation to investment management where downstream costs get netted off. Therefore the indicator doesn't give a level playing field when comparing direct and indirect investors.</p>
<p>C6. Do funds compete on costs/price?</p>	<p>Fees relative to assets and number of accounts by service (investment, administration and insurance services) and by market segment (output)</p>	<p>PC proposes using Regulator data; research firms; fund disclosures.</p>		<p>Fees can lack comparability both due to structure (e.g. flat dollar +% for some, pure % for others) and the netting off of costs and profit margin in underlying investments rather than using explicit fees. Note that any % fee includes an inbuilt escalation factor when FUM increases. PC should actively look for indications of % fees decreasing as FUM increases, or else commensurate increases in services. % fees permit some industry participants to capture the benefits of scale rather than passing them to members.</p>



<p>C6. Do funds compete on costs/price?</p>	<p>Fund margins (output)</p>	<p>PC proposes using Regulator data; research firms; fund disclosures.</p>		<p>Agree with this indicator We note there will be challenges with sourcing the data, especially from offshore suppliers (fund managers, custodians etc) who regard this information as confidential and prejudicial. Differences between P2M and for-profit sectors in net returns to members from products with similar risk attributes and/or strategic asset allocation would be a reasonable proxy for fund margins.</p>
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<p>C6. Do funds compete on costs/price?</p>	<p>Investment management costs and fees by asset class compared to other countries* (output)</p>	<p>PC proposes using research firms; fund disclosures</p>	<p>This is an important indicator of the efficiency of the Australian wholesale funds management sector compared with overseas counterparts, and the effectiveness of super trustees in extracting competitive pricing.</p> <p>The International Organisation of Pension Supervisors concluded in its IOPS Working Paper No 20 (April 2014) that “Comparing fees and charges across jurisdictions is a difficult task for a number of reasons:</p> <ul style="list-style-type: none"> - one challenge in such comparisons is the different reporting methods for fees and costs across jurisdictions, and the extent to which reported fees, costs and expenses include the same elements (e.g. fees charged by investment funds in a pension fund portfolio). - the structure of fees differs across jurisdictions. Pension funds may charge fees on assets under management, fees on flows, fees on contributions, fees on returns, fees on salaries etc. These expenses may be chargeable by differing parties (the fund, the administrator, other service providers) and paid by either the pension fund, the contributing member, an employer or out of underlying investment capital. <p>Since the designs of pension systems are different from one another, pension funds may be required to perform quite different tasks. Hence, fees and charges may be used to finance different services and/or products. This means that even where data may be comparable, raw figures might not accurately reflect whether fees are high or low. A higher fee could be explained because it is used not only to provide asset management services, but also collection, recovery and</p>
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			<p>payment services, unemployment or disability benefits, insurance, etc.”</p> <p>AIST notes that the way that investment fees are reported is influenced by the structure of the investment. According to Frontier Investment Advisors it costs more to manage alternative assets (e.g. an infrastructure asset), versus a portfolio of equities (e.g. an ASX 200 portfolio). However, listed markets contain alternative asset portfolios, such as infrastructure trusts, which are not declared on a look-through basis.</p> <p>For example, Macquarie Atlas Roads (MQA) is a constituent of the S&P/ASX 200:</p> <ul style="list-style-type: none"> . MQA pays the Manager, Macquarie, a base fee of 1.75% p.a. on the first \$1 billion of market capitalisation and 1% p.a. on amounts over \$1 billion (the current market cap. is circa \$1.5 billion) . It also pays Macquarie a performance fee if certain hurdles are met (last paid for the period ended 30 June 2011, with \$50.1 million paid to Macquarie in three instalments over 2011, 2012 and 2013) . If MQA were to be de-listed and managed by Macquarie in an unlisted vehicle, it would be expected that MySuper option would disclose the fees paid to Macquarie.
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Response to issues paper: Superannuation: Assessing Competitiveness and Efficiency, July 2017





<p>C6. Do funds compete on costs/price?</p>	<p>Alignment in the structure of member fees and underlying costs#* (output)</p>	<p>Fund surveys; regulator data; fund disclosures</p>		<p>Agree</p>
<p>C6. Do funds compete on costs/price?</p>	<p>Transparency and efficacy of fee disclosure by funds, including for distinct services# (behaviour)</p>	<p>Reviews by others</p>		<p>Again, AIST notes the capacity for funds to report low fees due to netting off costs from associated parties; for example, see Colonial Super Retirement Fund and MLC Retirement Fund cited in the body of the submission. After more than two years work, changes aimed at fuller reporting to better facilitate a member driven market for those willing and able to participate in one have not yet been agreed as part of ASIC's consultations on Regulatory Guide 97 (RG97), let alone implemented.</p>



<p>C7. Are economies of scale realised and the benefits passed through to members?</p>	<p>Unused scale economies at fund level* (output)</p>	<p>Regulator data; research firms</p>		<p>Estimations of unrealised scale benefits are important in assessing overall industry structure. See comments in the main submission. There is a significant international discussion on ‘unused scale economies’. Economies of scale may exhibit a U shaped average cost function. The range of factors that can impact on scale are diverse and there is uncertainty to the optimal size of a pension fund in the international context. Research indicates that many drivers of scale economy and optimal scale may change over time. There is a need for substantive work on the Australian system on optimal scale. AIST believes that this could be an area of future focus for the Commission, but at the current time when research on this issue is still developing this is not a workable indicator.</p>
<p>C7. Are economies of scale realised and the benefits passed through to members?</p>	<p>Entries, exits and consolidations of funds# (output)</p>	<p>Regulator data; fund disclosures</p>		<p>Entries and exits provide consistent, transparent measures and are indicators of an effective market at provider level. Fund consolidation is an important area (which PC may intend to restrict to mergers, but should extend to intra-fund consolidation) which is likely to be much more difficult because the extent of fragmentation within funds is less apparent. Consolidations WITHIN funds would be an important indicator, not only within master trusts where subplans with different features and pricing detract from scale benefits in terms of administration, but also in order to reduce excessive investment choice.</p>

<p>C7. Are economies of scale realised and the benefits passed through to members?</p>	<p>Pass through of benefits from scale economies (wholesale and retail) to members* (output)</p>	<p>Research firms; fund disclosures</p>	<p>Concerned that this is an ambiguous indicator. Probably neither consistent nor transparent, given the ways in which scale benefits can be applied - through reduced fees to members, improved services to members, increased returns to shareholders or enhanced benefits to fund management and employees.</p> <p>Economies of scale can result in reduced fees or increased services that include broader diversification. One of the implications of the maturing of the system is that superannuation funds need increased international diversification as the size of superannuation assets outgrows the size of the Australian economy. An assessment of economies of scale should be considered in context with the evolving nature of investment. Scale assessment should include the ability to provide services to members to help engagement and increase savings to support retirement goals.</p>
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<p>C7. Are economies of scale realised and the benefits passed through to members?</p>	<p>Increased diversification due to growing scale (input)</p>	<p>Research firms; fund disclosures</p>		<p>Agree with this indicator. One of the impacts of the maturing of Australia’s superannuation system is the need for superannuation funds to diversify. Funds have been increasing diversification for many years, with new asset classes evolving to embrace funds’ scale, sophistication and diversity. One of the implications of the growth of the size of the pool of superannuation assets is that superannuation assets are beginning to outgrow domestic assets. APRA regulated funds continued to see growth of assets over the last 2 ½ years with APRA data revealing that total assets increased from \$1.09 trillion in September 2013 to \$1.33 trillion in March 2016. The data is demonstrating that whilst Australian fixed income assets grew by 41%, Australian listed equity and Australian unlisted infrastructure assets grew by 12%. This compares to international investments which showed fixed income growing by 64%, international unlisted infrastructure by 363% and international listed equity 54%. The data demonstrate in graphic terms that investment offshore by superannuation funds is growing at a faster rate than investment in domestic assets. In simple terms, more superannuation capital is flowing offshore and is likely to continue to do so in coming years.</p>
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<p>C8. Do funds compete on member-relevant non-price dimensions?</p>	<p>Number of accumulation products (aggregate and per fund)* (output)</p>	<p>Regulator data</p>	<p>In terms of the overall criterion, AIST would argue that (with niche exceptions such as those prepared to sacrifice returns for non-financial considerations such as a religiously oriented fund) net returns at a given service level is the only legitimate consideration.</p> <p>On that basis AIST would see competition on non-price based factors as incidental.</p> <p>On the specific measure, the indicator will mean very different things in the accumulation phase compared to the retirement phase where product development is far less mature.</p> <p>If the assumption is that innovation is reflected in a greater number of products, and that more products lead to improved choice or alignment with member preference, the indicator is deeply flawed.</p> <p>Beyond an optimal number of distinct investment offerings within a fund, an increased number is likely to indicate excessive and inefficient choice. Greater choice does not lead to improved choice and better members' outcomes, especially for complex services like superannuation. There is ample psychological evidence that too many choices create confusion and have the effect of causing a person to avoid the confusion by not making a choice, and that complex choices are particularly challenging.</p> <p>The existence of different types of investment offering (e.g. lifecycle, enhanced lifecycle and standard accumulation) is likely to be indicative of genuine competition between funds, although the outcomes can't be clearly seen for decades.</p>
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<p>C8. Do funds compete on member-relevant non-price dimensions?</p>	<p>Fund marketing expenditure (share of operating expenditure) (input)</p>	<p>Regulator data; fund disclosures</p>		<p>Agree with this indicator. Maintaining and growing membership is necessary to obtain the benefits of scale. This should be measured relative to membership size and FUM, and separate from group marketing expenditure. However, available data is demonstrably inconsistent and opaque. APRA has only recently started collecting data on advertising expenditure, and published material shows clear inconsistencies. It also does not capture group expenditure that supports a super fund.</p>
<p>C8. Do funds compete on member-relevant non-price dimensions?</p>	<p>Funds' use of member information to inform product design and pricing* (input)</p>	<p>Fund surveys; case studies</p>		<p>AIST member funds report that they consistently use member data such as age cohorts, account balances and the current investment patterns of members to develop their key investment and insurance strategies. For example, one fund has an over-representation of female members of child-bearing age who take time out of the workforce, and so is particularly mindful of downside protection. Other funds provide varying insurance defaults tailored to the needs of members who are self-employed, or those likely to be in casual or contract employment who do not receive employment benefits like paid sick leave.</p>

<p>C8. Do funds compete on member-relevant non-price dimensions?</p>	<p>Availability of meaningful and comparable information on fees, product features (including insurance) and risks#* (input)</p>	<p>Reviews by others; member surveys</p>		<p>Agree with this indicator. In addition to investment risks, the Commission should focus on information provided to members that assists the member understanding changing capital market conditions and long term investment issues. Member surveys are unlikely to be reliable for this indicator, in that member perception is likely to be skewed by engagement. Thus not level playing field. Critical that member surveys stratify by characteristics such as age, gender, NESB, income and account balance. Of course, everyone conforms to PDS requirements, but the fact that most don't read those in detail if at all demonstrates how difficult this issue is. Difficulty in obtaining industry agreement on RG97 is also an indicator of difficulty in this space.</p>
<p>C8. Do funds compete on member-relevant non-price dimensions?</p>	<p>Member superannuation and insurance literacy#* (input)</p>	<p>Member surveys, fund disclosures and case studies</p>		<p>Unclear how member super and insurance literacy is an indicator of funds competition on non-price dimensions, though it may be an indicator of the (lack of) readiness of "the market" for such competition. Design of member survey will be critical in order to obtain any legitimate data. Note ANZ survey doesn't address insurance through super so that will need to be specifically addressed</p>


<p>C9. Is there innovation and quality improvement in the system?</p>	<p>Introduction of new retirement income products* (output)</p>	<p>Fund surveys; fund disclosures; case studies</p>		<p>We agree with the Commission in stating that “Ultimately, an assessment of the sector needs to go beyond a simple examination of product diversity and levels of uptake, and focus on market and policy barriers to product development and the implication of those barriers for competition and efficiency” (p223, Draft report No. 2)).</p> <p>We note that the interaction of superannuation, tax and social security law has been a significant impediment to the development of retirement income products. Recent rapid policy development in this, aimed at removing disincentives to developing new product types, has opened new possibilities. Work on CIPRs is a prime example.</p> <p>Whether or not funds offer retirement income products and/or have refined them in recent years is a consistent transparent measure and applicable across all funds. It doesn't necessarily yield "level playing field" results, in that funds with younger, low balance demographics will have less demand for them. Small funds will have little capacity to offer them. Aggregated industry data not readily available. APRA does not collect it; it offers only number of pension accounts opened in the reporting year.</p>
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<p>C9. Is there innovation and quality improvement in the system?</p>	<p>Development and active take-up of tailored products and member services* (output)</p>	<p>Fund surveys; fund disclosures; case studies</p>	<p>Concerned with the ambiguity of this indicator. The measure reflects the PC preference for a classic consumer driven market. The critical aspect is that fund knowledge of member characteristics is reflected in product and service design in both default and choice products. "Active take up" of such investment offerings is really only relevant in the choice space, though applies also where members retain an interest in a MySuper product as well as other choice options. A number of AIST funds report in excess of 90% of members in their MySuper product. This can be readily argued as an indicator of good product design meeting the needs of members. AIST notes anecdotal reports from funds of their members selecting choice investment options and later reverting to 100% investment in MySuper. AIST is concerned that the number of investment options in the non-MySuper space is primarily supply-driven and not member driven. While we anticipate innovation in retirement income products, it is not sufficient to say that an increase in the number of products indicates an innovative market and, where members lack confidence, reflect supply driven attempts at differentiation rather than genuine demand driven innovation. Increased products come at the cost of operational efficiency and higher fees to members.</p>
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<p>C9. Is there innovation and quality improvement in the system?</p>	<p>Introduction of new methods of service delivery* (output)</p>	<p>Fund surveys; fund disclosures; case studies</p>		<p>Funds which market on "bells and whistles" and large funds will have capacity and desire to develop "innovative service delivery mechanisms", even if this entails higher cost to members. Information not readily available. Query consistency as to what is "innovative".</p>
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<p>C10. Are outcomes improving at the system level?</p>	<p>Growing voluntary consumption of superannuation services (investment, retirement products, advice and insurance) (output)</p>	<p>Regulator data</p>	<p>Poor indicator.</p> <p>"Consumption of superannuation services" depends on member capacity and life circumstances. For example, increased casualisation of the workforce and reduced home ownership levels are likely to lead to increased demand for income protection insurance. Lower income earners won't generally have the capacity to make voluntary contributions. Exogenous factors like changed taxation for super may lead to increased demand for advice, but reduced contributions from higher income earners. The indicator also fails to acknowledge the inherent downsides of super (particularly preservation rules so far as younger and middle aged workers are concerned) and the substitutability of other savings vehicles.</p> <p>Possible proxy data would include after tax contributions, accessing advice from within fund (not collected by regulator), actively managing insurance (not collected by regulator), and taking benefit as income stream rather than lump sum.</p> <p>The focus by super funds to develop MySuper products to meet the needs of the largest cohort of their members may enable super fund members to receive the benefits of the super system without the need to consume additional services.</p> <p>A low level of consumption of additional services should improve efficiency where core services provide benefits that meet the needs and preferences of most members. This in turn reduces the costs in the system for services that are currently used to service needs for which the majority of super fund members do not demonstrate little demand. Accessible education and information provided by funds, whether by</p>
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				workplace seminar or websites, support members' decision making and improve financial literacy.
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<p>C10. Are outcomes improving at the system level?</p>	<p>Member satisfaction and trust* (outcome)</p>	<p>Member surveys</p>		<p>Concerned that this indicator is subject to fluctuations due to the volatility of investment markets. Historically member satisfaction increases when markets deliver strong investment returns and falls when markets drop. It would be useful to develop an indicator that was able to consider the impact of investment returns. Trust and satisfaction are very different things, which is evident in their measurement. Measures of satisfaction appear highly correlated to short term (six month) investment performance. Trust appears much more durable. This may be because while members may trust the super system and that trustees are acting in their best interests, they can still be unsatisfied with their performance due to global economic uncertainty and slowing rates of growth. We recommend measuring trust only. Trust measure also provides good cross-interpretation with engagement with respect to the coupling of high levels of trust with low levels of activity indicating and effective and efficiency operation of the trustee in designing default products.</p>
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<p>E1. Are long-term net investment returns being maximised over members' lifetimes, taking account of risk?</p>	<p>Long-term (5, 10 and 20 year) historical net investment returns from the system and market segments compared to benchmarks (output)</p>	<p>Regulator data; research firms</p>	<p>Agree with this indicator.</p> <p>Long-term net investment return is the fundamental criterion by which the system and each fund should be judged, especially from the perspective of default members given that many of these would rather have their SG contributions available for immediate consumption. Any additional services are genuinely ancillary, and should not detract materially from the overall retirement benefit.</p> <p>Note that net returns to members will also reflect the skill and diligence of trustees in managing costs at all levels, including taxation costs. It is the fundamental measure of the value added by trustees.</p> <p>APRA/ISC data provides whole of fund net returns over the reference periods. Whole of fund returns are the best available data sets over an extended period, and are a legitimate representation of the aggregate impact of:</p> <ul style="list-style-type: none"> • trustees selecting investment options to offer (including, importantly, the default option); • trustees managing costs; and • engaged members and their advisers acting in their assessed self-interest. <p>Arguments about older members choosing more conservative investment options simply demonstrate the failure of advisers to demonstrate to them the advantage of maintaining a significant proportion of growth assets in anticipation of life expectancy of 80+.</p> <p>There is very limited time series data for particular investment options, even defaults, and it is notable that, with the</p>
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			<p>introduction of MySuper and more extensive reporting, a significant proportion of commercial retail funds changed their default option to lifecycle, thus cancelling any continuing time series for them.</p> <p>We support the Commission’s requirement for two measures:</p> <ul style="list-style-type: none"> • The traditional CPI + x% over 5- 10- and 20- years measure is a familiar , easy-to-understand, headline measure which reflects members’ overall, CPI adjusted outcome. It provides Insight into whether funds’ Strategic Asset Allocation (SAA) have been successful <ul style="list-style-type: none"> o However, because the outcomes are dominated by market risk or beta, this measure does not provide substantial insight into Trustees’ investment skills; • Reference portfolios - “vanilla” lowest-cost form of delivering products in each prescribed risk category complement the CPI+ measures: <ul style="list-style-type: none"> o They give a much better reflection of the value-add by each fund relative to their SAA benchmark, o Reflect portfolio construction, selection of fund managers, use of private markets, etc. o Help to assess whether Trustees have used their resources (fees and skills) well and how they are rewarded over time o Reference portfolios provide a measure of the strength of investment craftsmanship. <p>Both measures have challenges with data quality/reporting by funds and ensuring that we compare apples with apples.</p> <p>We propose that a separate indicator be developed that assesses the degree to which the system is exercising ownership</p>
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				<p>rights that are conferred as an investor. This is expected to be a leading indicator of long term net returns and would be based around the significant body of work in responsible investment. Investors are exposed to long term risks that have the capacity to impact on long term investment returns.</p> <p>One example is climate change which, according to established science, will have significant environmental, social and economic impacts over the coming decades. Super funds have been actively engaged in assessing the risks of climate change on investment portfolios.</p> <p>Investors have also actively engaged on an international basis to develop corporate governance standards. Australian funds have taken a leadership role around corporate governance internationally including through legal cases that have established precedents around investor rights. In the Australian context super funds have been instrumental in the development of the ASX Corporate Governance Principles that are now in their third iteration. The ASX Corporate Governance Principles have significantly improved governance standards for ASX companies. Evidence suggests that there is a clear link between corporate governance and long term investment performance.</p>
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<p>E1. Are long-term net investment returns being maximised over members' lifetimes, taking account of risk?</p>	<p>Long-term (5, 10 and 20 year) historical net investment returns to specific asset classes from the system and market segments compared to benchmarks (output)</p>	<p>Regulator data; research firms</p>	<p>Agree with this indicator but care would need to be taken to measure returns net of both fees and tax, and to have regard to survivor bias when comparing funds' achieved returns by asset class against asset-based benchmarks like indices. AIST believes that indicators around long term investment are critical to provide an assessment of the efficiency of the superannuation system. In this regard it is important for the Commission to incorporate indicators that acknowledge the complexity of investment.</p> <p>The packaging of super as a product belies the fact that within each asset class there is significant complexity that investors must manage. Asset class benchmarks seek to capture relative performance and are commonly used by institutional investors as a tool to assess manager performance. However asset class benchmarks are only one component of a complex investment process.</p> <p>Other areas that should be captured in indicators are around changes to strategic asset allocation over time. Super funds may change strategic asset allocation for a number of reasons including that an asset class has become more expensive due to structural factors.</p> <p>In the case of infrastructure investments there is discussion as to whether increased prices that are currently being realised for mature infrastructure assets are cyclical or reflect a structural shift.</p> <p>At a system level new APRA data is revealing that international investments are growing at a faster rate than domestic investments. This reflects that in the early days of compulsory</p>
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			<p>superannuation there were sufficient investments available locally to absorb new contributions. As the size of the system has increased, the need for international diversification has also increased.</p> <p>AIST recommends that the Commission establishes indicators to focus on assessing the system’s ability to understand and manage change in investment markets over long time horizons. The exercise of ownership rights within funds’ investments would be expected to generate higher costs, but also higher rates of net return so the effect should be captured in a simple comparison of achieved net returns vs appropriate benchmarks. We note that some areas of investment are not well covered by asset-class benchmarks.</p> <p>We expect that over time super funds will invest in new assets that provide risk-adjusted returns, for which benchmarks may not exist.</p> <p>When assessing system level outcomes, the efficiency of the aggregate of choices made by individuals should be incorporated into the assessment. This is unlikely to be possible at product level, but demands that whole of fund returns be examined. In particular, if the aggregate of member choice (both within the institutional sector and for SMSFs) generates sub-optimal returns, that requires focus on each of members’ capacities to make choices; the role of trustees in putting various choice options on their menus and, especially, the role of advisers in influencing strategic asset allocations.</p> <p>It is also inappropriate for the PC to consider "institutional" funds as a whole, given the demonstrable difference in</p>
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				<p>outcomes achieved by P2M and commercial retail funds. There is unlikely to be sufficient longitudinal data for a realistic discussion of retirement products under this criterion, with most coming from AMP and Challenger, with some funded DB pension schemes also being available but having quite different characteristics from the annuity and developing account based pension elements.</p>
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<p>E1. Are long-term net investment returns being maximised over members' lifetimes, taking account of risk?</p>	<p>Proportion of default products that persistently underperform the benchmark (for 5 or more consecutive years) (output)</p>	<p>Regulator data; research firms</p>		<p>Supported. If the measure is to satisfy consistency and level-playing field norms, it must address default investment options within retail master trusts, not just the default option within default funds named in industrial awards and agreements. While there is no "default product" for SMSFs, it would be useful to compare the performance of the SMSF sector as a whole with defaults.</p>
<p>E2. Are costs incurred by funds and fees charged to members being minimised, taking account of service features provided to members?</p>	<p>Costs relative to assets and number of accounts by service (investment and administration) and by market segment (input)</p>	<p>Regulator data; research firms; fund disclosures</p>		<p>Agreed. However, AIST notes that costs incurred by a fund are frequently opaque, especially in the investment management space where they are typically netted off from declared returns. Fees charged to members can be disguised and manipulated, both by using a combination of flat rate and % fees and by using cross-subsidies, whether from particular employers or from within a vertically integrated business where the investment arm can finance aspects of the fund operation without an overt fee.</p>


<p>E2. Are costs incurred by funds and fees charged to members being minimised, taking account of service features provided to members?</p>	<p>Fees relative to assets and number of accounts by service (investment and administration) and by market segment (output)</p>			<p>Agreed with reservations.</p> <p>As noted by PC, this indicator does not lend itself to consistency (ATO and APRA require reporting on different bases for SMSFs and larger funds), transparency or level playing field. Fees charged to members can be disguised and manipulated, both by using a combination of flat rate and % fees and by using cross-subsidies, whether from particular employers or from within a vertically integrated business where the investment arm can finance aspects of the fund operation without an overt fee. Defining a service level as a benchmark will be difficult. PC notes the hope that tRG97 may address some of the inconsistencies into the future.</p> <p>Note also the capacity provided by many retail PDSs for funds to vary fees unilaterally across a very wide range; thus a client signing up at a point in time with a particular fee level won't know the likely fees to be charged into the future.</p>
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<p>E2. Are costs incurred by funds and fees charged to members being minimised, taking account of service features provided to members?</p>	<p>Investment management costs and fees by asset class compared to other countries* (output)</p>	<p>Research firms; fund disclosures</p>		<p>Agree with this indicator. AIST reiterates that care needs to be taken with international comparisons due to differences in systems, and lack of transparency in reported costs and structures. Note that, with increasing scale, Australian funds should be able to access international asset managers which in turn should lead to convergence of fees charged by Australian and international managers.</p>
<p>E2. Are costs incurred by funds and fees charged to members being minimised, taking account of service features provided to members?</p>	<p>Relationship between investment fees and returns at system level and for market segments (output)</p>			<p>Agree with this indicator. Market segmentation analysis is important for this indicator. Investment fees may be high due to asset allocation (especially to unlisted assets) or to high costs incurred where lower costs are available. The former case should generate positive net returns, while the latter won't.</p>

<p>E2. Are costs incurred by funds and fees charged to members being minimised, taking account of service features provided to members?</p>	<p>Cost savings from SuperStream (output)</p>	<p>Regulator data</p>	<p>Agree with this indicator. SuperStream should deliver efficiency for whole system. Administration fees for SMSFs should include all fees charged by accountants to manage SMSFs. SuperStream is a work in progress but is delivering efficiencies for the whole system, especially employers. Additional efficiencies should be obtained from implementation of single touch payroll, online new employee registration and new and expanded ATO reporting. The introduction of new payment platforms and integration of data and payment solutions will greatly improve the efficiency of the system. SuperStream has been implemented for rollovers and contributions from medium and large employers. The transition into SuperStream for small employers was scheduled to be completed on 28 October 2016. While super funds can be assessed on how well they implement these reforms, SuperStream benchmark reporting (APRA SRF 711.0) does not provide comparable information about cost savings from SuperStream. This is because each reporting super fund sets its own methodology. The capital cost of implementation by super funds, administrators, software developers, gateways, payroll providers, employers and the ATO should be considered in assessing cost savings to the system. It is likely that this has exceeded \$1 billion.</p>
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<p>E2. Are costs incurred by funds and fees charged to members being minimised, taking account of service features provided to members?</p>	<p>Relationship between level of administration fees and quality of member services (output)</p>	<p>Research firms; member surveys</p>		<p>AIST does not support this indicator as it is ambiguous and requires the Commission making judgements as to what is a “quality service”. Data reliability is questionable, but we note that research houses include quality factors in determining "fund of the year" etc. Equally relevant to SMSF sector but data from accountants etc. will be hard to come by. AIST notes research indicating that there was little evidence that higher fees correlate with better member service and concerns from the Cooper's review that many funds were providing higher levels of service, often unused by the great majority of members, at higher cost.</p>
<p>E2. Are costs incurred by funds and fees charged to members being minimised, taking account of service features provided to members?</p>	<p>Unused scale economies at fund level* (output)</p>	<p>Regulator data; research firms</p>		<p>Estimations of unrealised scale benefits are important in assessing overall industry structure. See comments in the main submission. There is a significant international discussion on ‘unused scale economies’. Economies of scale may exhibit a U shaped average cost function. The range of factors that can impact on scale are diverse and there is uncertainty to the optimal size of a pension fund in the international context. Research indicates that many drivers of scale economy and optimal scale may change over time. There is a need for substantive work on the Australian system on optimal scale. AIST believes that this could be an area of future focus for the Commission, but at the current time when research on this issue is still developing this is not a workable indicator.</p>



<p>E2. Are costs incurred by funds and fees charged to members being minimised, taking account of service features provided to members?</p>	<p>Pass through of benefits from scale economies (wholesale and retail) to members* (output)</p>	<p>Research firms; fund disclosures</p>		<p>Concerned that this is an ambiguous indicator. Probably neither consistent nor transparent, given the ways in which scale benefits can be applied - through reduced fees to members, improved services to members, increased returns to shareholders or enhanced benefits to fund management and employees.</p> <p>Economies of scale can result in reduced fees or increased services that include broader diversification. One of the implications of the maturing of the system is that superannuation funds need increased international diversification as the size of superannuation assets outgrows the size of the Australian economy. An assessment of economies of scale should be considered in context with the evolving nature of investment. Scale assessment should include the ability to provide services to members to help engagement and increase savings to support retirement goals.</p>
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<p>E2. Are costs incurred by funds and fees charged to members being minimised, taking account of service features provided to members?</p>	<p>Fee dispersion* (output)</p>	<p>Research firms; fund disclosures</p>		<p>This is a sound indicator of competition at the industry level; in a fully functional customer driven market, there would be little fee dispersion. Weakness is in the definition of fees, as discussed elsewhere. A greater dispersion between default and choice products does not necessarily indicate that a member is receiving enhanced services but may be an indication that a member is unaware of the impact of costs having been sold a product via a financial adviser. Dispersion could therefore be an indicator that providers are seeking to “game” the default fund selection system by churning members of default funds into higher fee products. In any event, the consideration of fees in isolation to net returns is concerning as it should not matter how products make their returns, just that they should be good after fees are taken into account.</p>
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<p>E3. Do all types of funds have opportunities to invest efficiently in upstream capital markets?</p>	<p>Asset allocation in small funds compared to large institutional funds (input)</p>			<p>Agree with this indicator.</p> <p>We note that asset allocation in SMSFs is not necessarily an indication of the availability of an investment opportunity. It may be an indication of investor education and behavioural bias. SMSFs have a wider investment universe than is being utilised. Of particular note, the ASX has enhanced the investment universe of SMSFs through developments including:</p> <ul style="list-style-type: none"> • Exchange-traded products (ETPs) – in recent years ASX has focused on increasing the number and range of ETPs. There are 176 ETPs listed on ASX totalling \$22.5 billion • Managed funds (fund) allows investors to apply for and redeem unlisted managed funds using their broker platform. At 30 June 2016, there were 161 funds <p>It is likely that over coming years the availability to access international markets will increase as ASX seeks opportunities in areas such as international equity warrants. There is likely to be a small number of assets which SMSFs do not have direct access to. There has been discussion on the fact that SMSFs cannot access unlisted infrastructure assets for instance. SMSFs are able to access infrastructure through listed companies and listed funds.</p> <p>In considering differences in asset allocation the Commission should develop mechanisms to strip out structures that are appropriate for institutional investors but not appropriate for small investors. The core question is whether SMSFs are able to gain exposure to similar assets from a risk / return perspective. Similarly there is no reason why small institutional funds should not be able to obtain the same gross investment returns as large</p>
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				<p>funds. Any failure to do so probably stems from inability to access scale efficiencies in terms of investment costs, and or lesser investment governance.</p>
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<p>E3. Do all types of funds have opportunities to invest efficiently in upstream capital markets?</p>	<p>Retail investment management costs compared to wholesale (input)</p>			<p>Agree with this indicator.</p>
<p>E3. Do all types of funds have opportunities to invest efficiently in upstream capital markets?</p>	<p>Minimum transaction values (input)</p>			<p>Agree with this indicator. The development of online broking services has enabled small investors to transact on capital markets at low cost.</p>
<p>E4. Is the system effectively managing tax for members, including in transition?</p>	<p>Average effective tax rates across market segments (output)</p>	<p>Regulator data; research firms</p>		<p>Appropriate only if asset allocations are comparable. However, a very useful indicator of the effectiveness of investment governance across sectors. Need to carve out insurance as a deductible since it is paid for separately. Otherwise, it is a useful and transparent indicator across segments, with data presumably available from the ATO.</p>

<p>E4. Is the system effectively managing tax for members, including in transition?</p>	<p>Tax flexibility as a motivation for establishing SMSFs (input)</p>	<p>Member surveys</p>		<p>Member surveys are likely to generate only self-serving data. The use of LRIVs to gear property, and the relatively extensive investment into private trusts suggests that SMSFs are quite often tax driven. That may be of value to the members of those SMSFs, but detrimental to the public interest at a system level.</p>
<p>E4. Is the system effectively managing tax for members, including in transition?</p>	<p>Take-up rates of co-contributions and offsets (input)</p>	<p>Regulator data</p>		<p>Data needed to properly interpret the headline data is unlikely to be readily available. Informative only if there is also information about the household income of those making use of these tax benefits. It is likely that they serve as tax management tools for the relatively wealthy, rather than as a means of enhancing gender equity or providing temporal smoothing in super.</p>

<p>E5. Are other leakages from members' accounts being minimised?</p>	<p>Unpaid Superannuation Guarantee contributions (input)</p>	<p>Regulator data</p>		<p>Agree with this indicator. However, current ATO data is poor, as demonstrated by the 2017 report of the Senate Economic References Committee. This measure could be largely addressed by the introduction of Single Touch Payroll, where employers submit PAYG and BAS records together with contributions information." The extent to which STP resolves unpaid SG depends on the extent of take up especially from small business, and the resources ATO is prepared to commit to pursuing unpaid super. They should - unpaid super is an early warning indicator of businesses in trouble and of unpaid taxes and potential phoenixing.</p>
<p>E5. Are other leakages from members' accounts being minimised?</p>	<p>Delayed Superannuation Guarantee contributions (input)</p>	<p>Regulator data</p>		<p>As above but ATO data is likely to be even more limited</p>
<p>E5. Are other leakages from members' accounts being minimised?</p>	<p>Number and value of lost accounts (output)</p>	<p>Regulator data</p>		<p>Agree with this indicator. System wide reforms should reduce the number of lost accounts. Anecdotally, a significant proportion of newly generated lost accounts stem from short term overseas visitors and workers in the cash economy.</p>



<p>E5. Are other leakages from members' accounts being minimised?</p>	<p>Trailing adviser commissions embedded in choice products and insurance# (output)</p>	<p>Fund surveys</p>		<p>Agree, but it is unlikely that relevant funds will be willing to disclose much in this space</p>
<p>E5. Are other leakages from members' accounts being minimised?</p>	<p>Unclaimed superannuation (output)</p>	<p>Regulator data</p>		<p>Source of unclaimed super will be relevant. Anecdotally a significant proportion these days is likely to come from the informal workforce, including those who have since departed Australia.</p>
<p>E6. Is the system providing high-quality information and intrafund financial advice to help members make decisions?</p>	<p>Availability of meaningful and comparable information on fees, product features (including insurance) and risks* (input)</p>			<p>AIST endorses this indicator but cautions that member perception of availability of information is likely to be skewed by engagement. Thus not level playing field. Critical that member surveys stratify by characteristics such as age, gender, NESB, income and account balance. Of course, everyone conforms to PDS requirements, but the fact that most don't read those in detail if at all demonstrates how difficult this issue is. Further, difficulty in gaining agreement on RG97 demonstrates fractured industry views.</p>

<p>E6. Is the system providing high-quality information and intrafund financial advice to help members make decisions?</p>	<p>Member active account activity:</p> <ul style="list-style-type: none"> • voluntary contributions • uptake of intrafund advice • changes to investment/insurance options* (input, behaviour) 	<p>Member surveys; fund disclosures; case studies</p>		<p>Voluntary contributions are restricted to those with spare savings capacity. APRA data shows numbers of members with MySuper interests as a result of investment choice; that should be a clear indicator of informed engagement.</p>
<p>E6. Is the system providing high-quality information and intrafund financial advice to help members make decisions?</p>	<p>Member account monitoring activity:</p> <ul style="list-style-type: none"> • use of fund websites • use of online calculators • call centre enquiries* (input, behaviour) 	<p>Member surveys; fund disclosures; case</p>		<p>Data is likely to be weak, especially with regard to channel. Member surveys highly unreliable, fund disclosures variable and highly aggregated where available, case studies selective. A selection of AIST member funds report between 4.8% and 10% member contacts in a month. Members with balances between \$100,000 and \$250,000 were by far the most likely to contact the fund; i.e. engagement increases with account balance. One fund reported that claims, pensions and inward rollovers were the most common reasons for contact.</p>


<p>E6. Is the system providing high-quality information and intrafund financial advice to help members make decisions?</p>	<p>Fund expenditure on member education and engagement as a proportion of total marketing expenditure* (input)</p>	<p>Research firms; fund disclosures; fund surveys</p>		<p>AIST considers this is an ambiguous indicator that depends on the definition of expenditure on member education and engagement, as well as on marketing. It is likely to be difficult to disaggregate data that is specifically targeted for member retention. We also note that it will be difficult to separately identify expenditure on “group” or brand advertising (e.g., in a multiple product financial conglomerate) from product or single super fund marketing expenditure. We are also uncertain what constitutes a “bad” score for this indicator. Is it a high spend? Member retention is needed as proof of competitiveness, as well as scale.</p>
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<p>E6. Is the system providing high-quality information and intrafund financial advice to help members make decisions?</p>	<p>Funds’ application of the lessons from behavioural finance to improve information provision and product design# (behaviour, output)</p>	<p>Case studies</p>	<p>The measure is ambiguous. The importance of ‘nudges’ to finance decisions is acknowledged. Nudges can be used in both positive and negative ways. In particular we note behavioural biases had a role to play in the establishment in the banking sector of late payment and overdrawn fees where the fees did not reflect the costs to the banks. The challenge with finance nudges is to ensure that they are done so in a way that is in the interests of members. In this regards simple measures, such as a binary question as to whether a provider utilised a nudge are potentially ambiguous. We note that behavioural finance lessons are being applied in communications, digital programs and interactive tools. These may be more relevant than products per se. We recommend amending this indicator to ensure that funds are measured in their application within the context of members’ best interests. This would ensure that the ability to exploit behavioural biases is explicit.</p>
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<p>E6. Is the system providing high-quality information and intrafund financial advice to help members make decisions?</p>	<p>Number of accumulation accounts and consolidations (behaviour, output)</p>	<p>Regulator data; member surveys</p>	<p>Agree with this indicator. Lost superannuation consolidation and reforms to SuperStream should lead to a consolidation of superannuation funds across the system.</p> <p>An efficient retirement savings system should protect against the erosion of members' capital through fees and charges. Similarly, an efficient system should discourage the duplication of fees and charges, particularly for consumers that are not actively choosing to participate in the retirement savings system.</p> <p>The Stronger Super package of reforms resulted in a requirement on super funds to implement their own policy on intra-fund consolidation, and thus reduce the number of duplicate accounts. Recent regulatory changes also allow Eligible Rollover Funds to undertake matching activities to assist with the reunification and consolidation of small, lost and unclaimed super accounts into active member accounts.</p> <p>In tandem with consolidation activities undertaken by the ATO, the successful implementation of these policies (including appropriate use of ERFs by super funds) could be used as assessment methods for this indicator.</p> <p>It would be very useful to have a time series showing the number of accounts for each TFN; given the increase in recent years of multiple part time or sequential short term jobs, the number of accounts per TFN should be increasing if all else were equal.</p>
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<p>E6. Is the system providing high-quality information and intrafund financial advice to help members make decisions?</p>	<p>Member superannuation and insurance literacy#* (input)</p>	<p>Member surveys, fund disclosures and case studies to provide evidence.</p>		<p>AIST does not accept that member superannuation and insurance literacy is an appropriate indicator of whether the system is providing high quality advice.</p>
<p>E7. Is the system providing products to help members manage risks over their life cycles and optimally consume their retirement incomes?</p>	<p>Asset allocations by age cohort (across different market segments and products) (output)</p>			<p>There is a vibrant debate across the superannuation industry on asset allocation as members age. There are a number of different approaches in the market. The presence of different approaches should be considered as an indication that different member preferences are being served in the market. Given the presence of different approaches in the market, an indicator around specific asset allocations by age would be ambiguous in terms of its meaning.</p> <p>In talking of members managing risks over their life cycles, is the PC putting itself forward as second guessing trustees as knowing what asset allocation is best for each market segment, age group and cohort? It is strongly arguable that existing commercial lifecycle products commence de-risking too early, which would clearly be an inefficient outcome. While we would expect to see more conservative asset allocations over the age</p>


				range 20-85, what benchmarks for suitability does the PC have in mind?
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<p>E7. Is the system providing products to help members manage risks over their life cycles and optimally consume their retirement incomes?</p>	<p>Life-cycle MySuper products (number of products and members, and as a proportion of total assets under management) (output)</p>	<p>Regulator data</p>		<p>MySuper products don't "help members manage risks over their lifecycle". Given that they are (generally) default products, they represent the trustee managing risk and return on behalf of the members.</p> <p>The inference that lifecycle products are superior is insidious, and a clear nudge in favour of the commercial retail funds which tend to offer them. An alternative interpretation as to why they offer them is to avoid comparison with single investment strategy outcomes, and with "competitors" offering different lifecycle products. Given longevity profiles, especially for higher balance members, there is a genuine risk that current lifecycle offerings de-risk way too early.</p>
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<p>E7. Is the system providing products to help members manage risks over their life cycles and optimally consume their retirement incomes?</p>	<p>Development and active take-up of tailored products and member services#* (output).</p>	<p>Fund surveys; fund disclosures; case studies</p>	<p>Concerned with the ambiguity of this indicator. The measure reflects the PC preference for a classic consumer driven market. The critical aspect is that fund knowledge of member characteristics is reflected in product and service design in both default and choice products. "Active take up" of such investment offerings is really only relevant in the choice space, though applies also where members retain an interest in a MySuper product as well as other choice options. A number of AIST funds report in excess of 90% of members in their MySuper product. This can be readily argued as an indicator of good product design meeting the needs of members. AIST notes anecdotal reports from funds of their members selecting choice investment options and later reverting to 100% investment in MySuper. AIST is concerned that the number of investment options in the non-MySuper space is primarily supply-driven and not member driven. While we anticipate innovation in retirement income products, it is not sufficient to say that an increase in the number of products indicates an innovative market and, where members lack confidence, reflect supply driven attempts at differentiation rather than genuine demand driven innovation. Increased products come at the cost of operational efficiency and higher fees to members.</p>
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<p>E7. Is the system providing products to help members manage risks over their life cycles and optimally consume their retirement incomes?</p>	<p>Introduction of new retirement income products#* (output)</p>	<p>Fund surveys; fund disclosures; case studies</p>		<p>We agree with the Commission in stating that “Ultimately, an assessment of the sector needs to go beyond a simple examination of product diversity and levels of uptake, and focus on market and policy barriers to product development and the implication of those barriers for competition and efficiency” (p223, Draft report No. 2)).</p> <p>We note that the interaction of superannuation, tax and social security law has been a significant impediment to the development of retirement income products. Recent rapid policy development in this, aimed at removing disincentives to developing new product types, has opened new possibilities. Work on CIPRs is a prime example.</p> <p>Whether or not funds offer retirement income products and/or have refined them in recent years is a consistent transparent measure and applicable across all funds. It doesn't necessarily yield "level playing field" results, in that funds with younger, low balance demographics will have less demand for them. Small funds will have little capacity to offer them. Aggregated industry data not readily available. APRA does not collect it; it offers only number of pension accounts opened in the reporting year.</p>
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<p>E7. Is the system providing products to help members manage risks over their life cycles and optimally consume their retirement incomes?</p>	<p>Funds' use of member information to inform product design and pricing#* (input)</p>	<p>Fund surveys; case studies</p>		<p>AIST member funds report that they consistently use member data such as age cohorts, account balances and the current investment patterns of members to develop their key investment and insurance strategies. For example, one fund has an over-representation of female members of child-bearing age who take time out of the workforce, and so is particularly mindful of downside protection. Other funds provide varying insurance defaults tailored to the needs of members who are self-employed, or those likely to be in casual or contract employment who do not receive employment benefits like paid sick leave.</p>
<p>E7. Is the system providing products to help members manage risks over their life cycles and optimally consume their retirement incomes?</p>	<p>Member superannuation and insurance literacy#* (input)</p>	<p>Member surveys, fund disclosures and case studies to provide evidence.</p>		<p>Unclear how member super and insurance literacy is an indicator of funds providing products to help members manage risks. It may be an indicator of the need for trustees to design high quality default products to cater for the needs of members who do not have a high level of financial literacy. Design of member survey will be critical in order to obtain any legitimate data. Note ANZ survey doesn't address insurance through super so that will need to be specifically addressed</p>

<p>E8. Are principal-agent problems being minimised?</p>	<p>Existing ratings of system-wide quality of governance (input)</p>	<p>Reviews by others</p>		<p>AIST agrees with this indicator but is concerned that it allows for very selective presentation by the Commission. For example, if they accept the conventional wisdom that the number of independents is a positive indicator of quality, the equal representation model will be rejected notwithstanding the demonstrated outperformance of P2M funds with equal representation boards.</p> <p>Indicators should include diversity, including the number of women and other groups on trustee boards; there is a significant body of work on the benefits of diversity in terms of corporate performance.</p>
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<p>E8. Are principal-agent problems being minimised?</p>	<p>Meaningful disclosure by trustee boards of trustee directors' and investment committee members' qualifications and relevant skills/experience; remuneration; potential conflicts of interest due to related-party dealings and competing duties (behaviour)</p>	<p>Reviews by others</p>		<p>AIST supports the minimisation of principal-agent problems. We note that disclosure of director and investment committee members experience is mandated, and AIST has gone further with its Code of Governance for member funds. The measure is a process one for which data is not readily available. The evidence of the quality of governance is the distribution of net returns to members, and on that basis the different skill sets around the table in equal representation funds have historically outperformed the professional directors and executive directors typically used in commercial retail funds. AIST flags issues of intractable conflicts for executive directors, and notes research supporting broadening the skills and experience of boards. We also point out the proportion of AIST member funds which have had directors participate in AIST's trustee director training.</p>
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<p>E8. Are principal-agent problems being minimised?</p>	<p>Quality of investment committee and investment governance processes, including use of performance attribution analysis and risk management (input)</p>	<p>Reviews by others; fund surveys</p>	<p>This indicator is already covered by legislation and standards. APRA has determined that super funds must establish an investment governance framework (Prudential Standard SPS 530). An investment governance framework is defined as the totality of systems, structures, policies, processes and people to address the RSE licensee’s responsibilities with regard to investments of each RSE within the RSE licensee’s business operations. This includes generating returns to meet investment objectives while managing and monitoring all identified sources of investment risk.</p> <p>An indicator that focuses on “level of skills and standard of performance” is likely to be subjective and is not consistent with APRA’s Investment Governance standard.</p> <p>In relying on research by others, AIST expects that the Commission will have regard to research/reviews supporting the quality of investment processes in profit-to-member funds in Australia and internationally.</p> <p>Note that the relative performance of P2M funds in Australia in generating strong net returns to members demonstrates the effectiveness of their investment governance processes.</p>
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<p>E8. Are principal-agent problems being minimised?</p>	<p>Member satisfaction and trust* (outcome)</p>	<p>Member surveys</p>	<p>Concerned that this indicator is subject to fluctuations due to the volatility of investment markets.</p> <p>As previously noted, historically member satisfaction increases when markets deliver strong investment returns and falls when markets drop. It would be useful to develop an indicator that was able to consider the impact of investment returns.</p> <p>Trust and satisfaction are very different things, which is evident in their measurement. Measures of satisfaction appear highly correlated to short term (six month) investment performance. Trust appears much more durable. This may be because while members may trust the super system and that trustees are acting in their best interests, they can still be unsatisfied with their performance due to global economic uncertainty and slowing rates of growth.</p> <p>We recommend measuring trust only.</p> <p>Trust measure also provides good cross-interpretation with engagement with respect to the coupling of high levels of trust with low levels of activity indicating an effective and efficient operation of the trustee in designing default products – especially when the proportion of members who can be shown to have actively selected the default MySuper option is considered.</p>
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<p>E8. Are principal-agent problems being minimised?</p>	<p>Proportion of complaints to the Superannuation Complaints Tribunal which are successful# (output)</p>	<p>Regulator data</p>		<p>This is a legitimate indicator of members' reasonable dissatisfaction with funds. It would be improved if the denominator included complaints made but subsequently withdrawn prior to SCT decision.</p>
<p>E8. Are principal-agent problems being minimised?</p>	<p>Proportion of funds that target short-term performance relative to their peers (behaviour)</p>	<p>Research firms; fund disclosures; fund surveys</p>		<p>Very few funds would include this as an explicit objective, though quite a lot include something along the lines of "maintain top quartile/above average net returns." The behaviour of funds suggests that most have regard to performance relative to peers - that is the whole basis of much work from ratings agencies.</p>
<p>E8. Are principal-agent problems being minimised?</p>	<p>Degree of similarity in asset allocation among default products with different member characteristics (average age and balance) (input)</p>			<p>Default product asset allocation is an important function of trustees. Differentiation is not necessarily an indicator of principal-agent problems.</p>


<p>E9. Does the system overcome impediments to improving long-term outcomes for members?</p>	<p>Introduction of new retirement income products#* (output)</p>			<p>We agree with the Commission in stating that “Ultimately, an assessment of the sector needs to go beyond a simple examination of product diversity and levels of uptake, and focus on market and policy barriers to product development and the implication of those barriers for competition and efficiency” (p223, Draft report No. 2)).</p> <p>We note that the interaction of superannuation, tax and social security law has been a significant impediment to the development of retirement income products. Recent rapid policy development in this, aimed at removing disincentives to developing new product types, has opened new possibilities. Work on CIPRs is a prime example.</p> <p>Whether or not funds offer retirement income products and/or have refined them in recent years is a consistent transparent measure and applicable across all funds. It doesn't necessarily yield "level playing field" results, in that funds with younger, low balance demographics will have less demand for them. Small funds will have little capacity to offer them. Aggregated industry data not readily available. APRA does not collect it; it offers only number of pension accounts opened in the reporting year.</p>
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<p>E9. Does the system overcome impediments to improving long-term outcomes for members?</p>	<p>Development and active take-up of tailored products and member services#* (output)</p>	<p>Fund surveys; fund disclosures; case studies</p>	<p>Concerned with the ambiguity of this indicator. The measure reflects the PC preference for a classic consumer driven market. The critical aspect is that fund knowledge of member characteristics is reflected in product and service design in both default and choice products. "Active take up" of such investment offerings is really only relevant in the choice space, though applies also where members retain an interest in a MySuper product as well as other choice options. A number of AIST funds report in excess of 90% of members in their MySuper product. This can be readily argued as an indicator of good product design meeting the needs of members. AIST notes anecdotal reports from funds of their members selecting choice investment options and later reverting to 100% investment in MySuper. AIST is concerned that the number of investment options in the non-MySuper space is primarily supply-driven and not member driven. While we anticipate innovation in retirement income products, it is not sufficient to say that an increase in the number of products indicates an innovative market and, where members lack confidence, reflect supply driven attempts at differentiation rather than genuine demand driven innovation. Increased products come at the cost of operational efficiency and higher fees to members.</p>
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<p>E9. Does the system overcome impediments to improving long-term outcomes for members?</p>	<p>Introduction of new methods of service delivery* (output)</p>	<p>Fund surveys; fund disclosures; case studies</p>		<p>Funds which market on "bells and whistles" and large funds will have capacity and desire to develop "innovative service delivery mechanisms", even if this entails higher cost to members. Information not readily available. Query consistency as to what is "innovative".</p>
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<p>E9. Does the system overcome impediments to improving long-term outcomes for members?</p>	<p>Number of accumulation products (aggregate and per fund)* (output)</p>	<p>Regulator data</p>	<p>In terms of the overall criterion, AIST would argue that (with niche exceptions such as those prepared to sacrifice returns for non-financial considerations such as a religiously oriented fund) net returns at a given service level is the only legitimate consideration.</p> <p>On that basis AIST would see competition on non-price based factors as incidental.</p> <p>On the specific measure, the indicator will mean very different things in the accumulation phase compared to the retirement phase where product development is far less mature.</p> <p>If the assumption is that innovation is reflected in a greater number of products, and that more products lead to improved choice or alignment with member preference, the indicator is deeply flawed.</p> <p>Beyond an optimal number of distinct investment offerings within a fund, an increased number is likely to indicate excessive and inefficient choice. Greater choice does not lead to improved choice and better members' outcomes, especially for complex services like superannuation. There is ample psychological evidence that too many choices create confusion and have the effect of causing a person to avoid the confusion by not making a choice, and that complex choices are particularly challenging.</p> <p>The existence of different types of investment offering (e.g. lifecycle, enhanced lifecycle and standard accumulation) is likely to be indicative of genuine competition between funds, although the outcomes can't be clearly seen for decades.</p>
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<p>E9. Does the system overcome impediments to improving long-term outcomes for members?</p>	<p>Funds' application of the lessons from behavioural finance to improve information provision and product design# (behaviour, output)</p>	<p>Case studies</p>		<p>The measure is ambiguous. The importance of 'nudges' to finance decisions is acknowledged. Nudges can be used in both positive and negative ways. In particular we note behavioural biases had a role to play in the establishment in the banking sector of late payment and overdrawn fees where the fees did not reflect the costs to the banks. The challenge with finance nudges is to ensure that they are done so in a way that is in the interests of members. In this regards simple measures, such as a binary question as to whether a provider utilised a nudge are potentially ambiguous. We note that behavioural finance lessons are being applied in communications, digital programs and interactive tools. These may be more relevant than products per se. We recommend amending this indicator to ensure that funds are measured in their application within the context of members' best interests. This would ensure that the ability to exploit behavioural biases is explicit.</p>
<p>E9. Does the system overcome impediments to improving long-term outcomes for members?</p>	<p>Impact of regulatory impediments on innovation (input)</p>	<p>Case studies</p>		<p>As noted above, regulatory mismatches have impeded the development of retirement income products. Extensive grandfathering and concessions in respect of choice products have permitted high cost, low value products to remain in the system, where a more active regulatory stance would have promoted innovation and reduced costs overall.</p>




<p>E10. Are there material systemic risks in the superannuation system?</p>	<p>Market concentration at wholesale and retail levels (Herfindahl-Hirschman Index and market shares of largest providers)* (output)</p>	<p>Regulator data</p>		<p>Agree with this indicator, although we think it is likely to be of limited use in the super funds sector of the system. The collective market share of the largest firms in the industry is likely to increase in the short term through industry consolidation. In the long term it is desirable that there is a diversity of providers. The HHI will be more relevant in measuring concentration in custody and administration services where the systemic risk is likely to be concentrated though it is unlikely that data will be available in respect of them.</p>
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<p>E10. Are there material systemic risks in the superannuation system?</p>	<p>Degree of interconnectedness between upstream service providers and funds (input)</p>			<p>Agree with this indicator. AIST proposes that in addition to the two indicators proposed, the Commission should consider indicators that assess the degree to which individual super funds adopt similar investments that have the potential to lead to increased systemic risks. There are two useful examples: If super funds were to shift to collectively to passive management of Australian shares this would potentially lead to concentration risks. There is evidence that increased passive investment may have impacts on market volatility. The second example is if SMSFs moved significantly into a particular asset class. This could overheat a market, as has arguably already happened in the residential property market, but would also have implications from the withdrawal from existing assets. The large proportion of SMSF investments in bank deposits for instance could be impacted which would have systemic impacts due to the importance of deposits for bank funding under Basel III</p>
<p>E10. Are there material systemic risks in the superannuation system?</p>	<p>Levels of leverage in SMSFs (input)</p>			<p>Whilst we agree with this indicator, we recommend that it be modified to take into account current and intended levels of leverage in superannuation system. We note that intended future leverage has been linked to SMSF establishment as a material driver of activity.</p>




<p>E11. Do funds offer value for money insurance products to members?</p>	<p>Duplicate insurance policies (output)</p>	<p>Member surveys</p>		<p>Likely to be a very poor indicator of the number of duplicate policies, because most who have them won't know about it. Virtually irrelevant to the issue of whether the insurance products that are offered represent value of money. AIST considers the optimal system-wide result is one insurance policy for each super fund member (that is, not for each account). There should also be near universal insurance coverage – excepting only those who have opted-out of insurance cover, or have actively sought additional cover. This widespread coverage is a benefit of the default death and TPD insurance built into the infrastructure for MySuper products. This design has enabled many Australians to access default insurance that is affordable, and in many cases, tailored to their demographic.</p>
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<p>E11. Do funds offer value for money insurance products to members?</p>	<p>Rates of insurance take-up in choice products relative to default products (output)</p>	<p>Regulator data; research firms</p>		<p>We do not agree with this indicator which again reflects a real weakness from PC in confusing products and accounts. If a member has investment in 4 different choice products, and has insurance, is that insurance associated with each of the products? And if they have some money in a MySuper account as well, how are their circumstances to be assessed?</p> <p>Members with MySuper products can and do elect to purchase additional or differently structured insurance from the default insurance arrangements. A comparison of insurance in choice products and SMSFs with that of default products does not therefore provide useful information about insurance take up rates.</p> <p>As many consumers of choice products and SMSFs are advised into taking additional insurance without necessarily understanding the cover purchased, this is also not an effective gauge of engagement.</p>
<p>E11. Do funds offer value for money insurance products to members?</p>	<p>Member superannuation and insurance literacy##* (input)</p>	<p>Member surveys, fund disclosures and case studies</p>		<p>Member literacy is not an indicator of whether trustees acting in member interests are actually providing value for money insurance products to members. It is actually a measure of trustee value-add that members actually receive good value for money insurance despite being unaware of their needs.</p>

<p>E11. Do funds offer value for money insurance products to members?</p>	<p>Ease of members opting out of insurance, amending cover or making claims (input)</p>	<p>Member surveys; reviews by others</p>		<p>Member surveys won't generate the required data because most have never done any of the measured things. It means that any in the sample who have done those things will carry a disproportionate weight in the results. This criterion lends itself to anecdotal reporting, and that will be overwhelmingly negative because those with good experiences tend not to volunteer them.</p> <p>Some AIST member funds report that on-line opt-out instructions are acceptable while others require hard copy. There is an element of risk management in this, to minimise the risk that a member may opt out and subsequently claim on the policy, arguing that the opt out was inadvertent or not fully informed.</p>
<p>E11. Do funds offer value for money insurance products to members?</p>	<p>Number of members changing or opting out of default insurance cover (input)</p>	<p>Research firms</p>		<p>The indicator has some merit as a measure of member engagement and fund openness to assist them. Of course, if the default settings are good for the great majority of members, there will be few seeking to change them.</p>

<p>E11. Do funds offer value for money insurance products to members?</p>	<p>Funds' use of member information to inform product design and pricing#* (input)</p>	<p>Fund surveys; case studies</p>		<p>AIST member funds report that they consistently use member data such as age cohorts, account balances and the current investment patterns of members to develop their key investment and insurance strategies. For example, one fund has an over-representation of female members of child-bearing age who take time out of the workforce, and so is particularly mindful of downside protection. Other funds provide varying insurance defaults tailored to the needs of members who are self-employed, or those likely to be in casual or contract employment who do not receive employment benefits like paid sick leave.</p>
<p>E11. Do funds offer value for money insurance products to members?</p>	<p>Comparability of insurance product information disclosed by funds (input)</p>	<p>Reviews by others; research firms</p>		<p>Agree with this indicator. PC should engage researchers to review insurance disclosures in PDSs.</p>
<p>E11. Do funds offer value for money insurance products to members?</p>	<p>Average insurance cover by age band and market segment (output)</p>	<p>Research firms</p>		<p>Tailoring of insurance products by particular member types means that the averages will have little meaning in assessing whether products offered represent value for money.</p>

<p>E11. Do funds offer value for money insurance products to members?</p>	<p>Proportion of complaints to the Superannuation Complaints Tribunal which are successful# (output)</p>	<p>Regulator data</p>		<p>Highly inappropriate indicator for this criterion, unless it is refined to relate only to insurance related complaints.</p>
<p>E11. Do funds offer value for money insurance products to members?</p>	<p>Number of members that nominate beneficiaries (input)</p>	<p>Member surveys; fund surveys; research firms</p>		<p>The indicator won't be equal across sectors, in that advised members would be expected to almost always nominate a beneficiary whereas there's not the personal contact at the point of signing up a default member to ensure that this occurs.</p>
<p>E12. Are the costs of insurance being minimised for the level and quality of cover?</p>	<p>Insurance premiums inside compared to outside superannuation for like policies (output)</p>	<p>Insurer disclosures; research firms</p>		<p>Agree with this indicator provide that it is benchmarked against minimum service standards for the industry. "Like for like" may be an issue, given that members in commercial retail funds are far more likely to be subject to high cost underwriting than is the case in profit-to-member funds.</p>

<p>E12. Are the costs of insurance being minimised for the level and quality of cover?</p>	<p>Insurance expenses (incurred by funds) (input)</p>	<p>Regulator data; fund surveys</p>		<p>Agree with this indicator provide that it is benchmarked against minimum service standards for the industry. Ensure that "expenses borne by funds" are gross of any employer subsidies.</p>
<p>E12. Are the costs of insurance being minimised for the level and quality of cover?</p>	<p>Insurance premiums paid by members as a percentage of Superannuation Guarantee contributions made by insured members (output)</p>	<p>Regulator data</p>		<p>Strongly agree with this indicator.</p>
<p>E12. Are the costs of insurance being minimised for the level and quality of cover?</p>	<p>Ratio of claims to premium revenue (loss ratio) within superannuation over 5 and 10 year periods (output)</p>	<p>Regulator data</p>		<p>Strongly agree with this indicator.</p>

<p>E12. Are the costs of insurance being minimised for the level and quality of cover?</p>	<p>Fee and premium differences from outsourcing insurance services to related versus unrelated parties (output)</p>	<p>Fund surveys; regulator data; fund disclosures</p>		<p>Agree with this indicator. Should also include information about fund practices around default characteristics (e.g. smoker/non-smoker, exclusions), what happens when contributions aren't being received, circumstances in which insurance cover is suspended or cancelled, details of any profit share arrangements, duration of contract, frequency of market testing especially where related party insurers are used.</p>
<p>E12. Are the costs of insurance being minimised for the level and quality of cover?</p>	<p>Proportion of APRA-regulated institutional funds switching their insurance provider (input)</p>	<p>Fund disclosures</p>		<p>This number will be too low in any year to provide meaningful insight. It should be assessed over the previous 5 years, and should be supplemented by funds going out to tender for insurance in the past 5 years, irrespective of whether they changed insurer. Data should be reported by the Productivity Commission based on profit-to-member vs commercial retail and for SMSFs.</p>
<p>E12. Are the costs of insurance being minimised for the level and quality of cover?</p>	<p>Trailing adviser commissions embedded in choice products and insurance# (output)</p>	<p>Fund surveys</p>		<p>Unlikely that relevant funds will be willing to disclose much in this space</p>