

13 April 2012

Mike Woods  
Deputy Chairman  
Productivity Commission  
LB2 Collins St East  
Melbourne VIC 8003

Dear Deputy Chairman,

## Default Superannuation Funds in Modern Awards

Colonial First State (CFS) is one of Australia's largest wealth management organisations with over \$73 billion in funds under management and a retail market share of around 15%, across the Commonwealth Bank Group.<sup>1</sup> CFS offers investment, superannuation and retirement products. In addition, we have six financial advisory networks in Commonwealth Financial Planning, Financial Wisdom, Whittaker Macnaught, BW Financial Advice, Advice Essentials and Count Financial Group. Our flagship platform, FirstChoice, is the largest investment platform in the Australian market with \$50 billion in funds under management and includes our retail corporate superannuation product, FirstChoice Employer Superannuation which operates in the employer superannuation market. FirstChoice Employer Super has around \$5 billion in funds under administration and over 7,700 employer plans and 240,000 members.<sup>2</sup>

CFS has long been a market leader in platform pricing and service. For example, our FirstChoice Wholesale product has a total weighted average product fee of just 0.76% (including administration and investment fee components but not including any agreed advice fees). The platform provides leading administrative speed and efficiency that means clients can transact today and receive a confirmation tomorrow. CFS's FirstWrap and FirstChoice have been ranked No.1 and No.2 respectively by advisers, for overall satisfaction in the 2011 Wealth Insights Service Level Survey.<sup>3</sup>

## Introduction

CFS is highly supportive of this review and appreciates the opportunity to contribute to the development of appropriate settings for the default superannuation market. We do not attempt to answer each question in the issues paper and instead focus on the rationale we believe should underlie the default fund selection process given the establishment of MySuper. CFS strongly

<sup>1</sup> Plan for Life, administrator view, June 2011

<sup>2</sup> As at February 2012

<sup>3</sup> Wealth Insights 2011 Platform Service Level Report and survey of 867 aligned and non-aligned advisers Mar/Apr 2011

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endorses the FSC submission on this matter including its full set of recommendations.

The review is critical to ensure similar levels of transparency and accountability apply to all parties involved in the default fund selection process as those soon to be applicable to MySuper trustees. It is in that light that CFS welcomes statements by the Productivity Commission suggesting the review will not be limited by the Government's terms of reference<sup>4</sup>. In our view such an approach is necessary to ensure adequate transparency and accountability and to ensure best outcomes for members.

### **Current Settings – The Role of Industrial Awards**

The *Fair Work Act 2009* included the Government's safety net amendments combining a set of national employment standards with the modernisation of awards, both effective from 1 July 2010. As part of award modernisation, superannuation became a matter that could be specified within each modern award.

Under the award modernisation process modern awards created by the Fair Work Australia (FWA) identify a limited number of specific superannuation funds (and in some cases one fund) which can be a default fund in a particular industry. This means employers with award employees will have a very limited choice of funds unless they can strike an industrial agreement with employees to install a different default fund.

This has led to a lack of competition and stagnation of the default superannuation market. Specifying individual default funds in awards and thereby creating effective oligopolies / monopolies for certain funds has reduced the overall level of competition in the sector. This has led to an upward impact on fees for these funds and resulted in reduced quality of products and services for members. As a result of these arrangements the vast majority of award employees are unable to access the benefits of a sector that has become increasingly competitive. CFS believes these arrangements are restrictive, anti-competitive and compromise the best interests of employees and members.

Contrast this to the situation where an employer has non-award employees and is free to select its own default fund. Employers typically receive advice from consultants and/or financial advisers to assist them select an appropriate fund. As part of the selection process a number of criteria are generally considered including pricing (fees), selection of investment options, strength of brand, insurance premiums and coverage, education, member service and access to financial advice etc.

The fund selection process is generally completed through a competitive tender which results in better member outcomes. The level of competition in the employer superannuation market is evidenced by the level of average fees in this sector of the market. Rice Warner Actuaries, in its Superannuation Fees Report 2008, shows that the average total fees for large corporate superannuation master trusts were 0.79%, well below the overall average of 1.21%. Regrettably, these funds are generally excluded from being default funds for award employees.

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<sup>4</sup> Senate Economics Legislation Committee, Thursday 16 February 2012, Proof Hansard p. 114

CFS believes better member retirement outcomes can be achieved through increased transparency and competition in the default superannuation sector. We think the best way to facilitate this is through the application of market forces aligned with the principles established via the Government's MySuper policy.

It is on this basis that CFS recommends removing the ability of awards to specify default funds, allowing employers the freedom to select an APRA approved MySuper default fund based on their own consideration of the merits of each fund.

### **Future State - A new default superannuation market, MySuper**

It is important to highlight that the very nature of the default fund market will be dramatically altered following the establishment of MySuper. In the words of Minister Shorten,

*"MySuper will provide a simple, cost-effective default product that all Australians can rely upon"*<sup>5</sup>

CFS agrees with the Minister and suggests this is particularly so given the features of MySuper as outlined below. These features underpin the reliance to which the Minister refers, allowing employers to feel safe and secure when selecting an APRA approved MySuper product as their default fund:

- APRA approval process - all MySuper products will be passed through the fine filter of APRA approval ensuring they meet the relevant standards. APRA are the gatekeeper of the new default market and have the power to ensure that any product or trustee who does not meet the strict criteria is restricted from operating.
- Highly regulated, comparable products – all MySuper products will be required to meet strict standards with respect to fees, investment strategies, insurance settings and the provision of additional member services. APRA will collect and collate data and publish league tables to assist employers when determining the appropriateness of MySuper offerings.
- Higher trustee duties – all trustees who offer a MySuper product will have increased duties and obligations over and above those applicable to trustees operating solely in the superannuation choice sector. This includes for example the requirement to promote the financial interests of MySuper members and include in the investment strategy an investment return target.
- Scale – all MySuper trustees will be required to determine whether the fund has sufficient scale to continue to act in the best interests of members.

The Parliamentary Joint Committee on Corporations and Financial Services (PJC) recognise the significant standards to be met not only by MySuper products but, just as importantly, by the trustees who issue them,

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<sup>5</sup> The Hon. Bill Shorten MP, Minister for Financial Services and Superannuation, *House of Representatives Hansard*, 3 November 2011, pp. 12683 - 12684

*".....the definition of 'MySuper product' encompasses not only the characteristics of the product but also the 'likely' actions of the product provider."*<sup>6</sup>

*"Additional obligations will be introduced in respect of trustees that offer MySuper products. This reflects the unique nature of MySuper as a default product; as noted by the Minister in his second reading speech, members of MySuper products 'have effectively delegated all decisions for their superannuation to the trustee'."*<sup>7</sup>

### **MySuper – an appropriate universal default product**

Your issues paper states "the Commission will consider whether to allow all MySuper products to be eligible for nomination in modern awards, or whether there is a net benefit to designing criteria over and above those for MySuper."<sup>8</sup>

CFS believes that the Cooper Review process culminating in the Government's Stronger Super Proposals and legislation recently reviewed by the PJC has designed in great detail appropriate criteria for default fund selection. As just discussed, those criteria are embodied in MySuper and in and of itself forms sufficient selection criteria.

In fact the introduction of additional criteria could have unintended and negative consequences upon the new default superannuation market:

- Undermining public confidence in MySuper – if only certain MySuper funds are appropriate for selection in Modern Awards, arguably, those MySuper funds that are not appropriate could be considered flawed or inferior. Indeed, the rationale for MySuper itself (as currently constructed) would be called into question.
- Undermining APRA's role – a significant element of the Government's Stronger Super reforms is APRA's role in the creation and on-going monitoring of trustee obligations and standards, including those applicable to MySuper. Separate criteria may potentially erode the work being done by APRA to ensure all default members receive adequate protections. It would also result in unnecessary and costly duplication of oversight responsibilities.
- Increased Regulatory Burden - given the strict and appropriate criteria designed by the Government for MySuper and the legislation requiring that only MySuper compliant funds and trustees operate in the default space, it may be considered onerous and burdensome to have a further subset of requirements for selection in Modern Awards.
- A failure to address existing competition issues in the default market by creating a two-tiered system.

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<sup>6</sup> Parliamentary Joint Committee on Corporations and Financial Services, Report on MySuper Core Provisions Bill 2011 and Trustee Obligations and Prudential Standards Bill 2012 p.16, March 2012

<sup>7</sup> Parliamentary Joint Committee on Corporations and Financial Services, Report on MySuper Core Provisions Bill 2011 and Trustee Obligations and Prudential Standards Bill 2012 p.22, March 2012

<sup>8</sup> Default Superannuation Funds in Modern Awards, Productivity Commission Issues Paper p.2, February 2012

## **Competition – the missing link**

CFS contends that whilst MySuper will itself provide a simple, cost effective, default superannuation product the full benefits of MySuper and the best interests of members can only be realised in an open and competitive marketplace. We agree with the following views,

*"Coalition members of the Committee are of the view that in creating this new default superannuation product, all MySuper funds should be allowed to be an eligible default fund for any workplace and be able to compete freely. To not allow MySuper funds to compete on a level playing field fails to address the existing competition issues in the default super industry and undermines the MySuper reforms."<sup>9</sup>*

The benefits to members of heightened regulation and homogeneity in the MySuper market combined with competitive forces are also alluded to by the PJC,

*"The committee acknowledges the concerns of some organisations that the MySuper product cannot be tailored to different parts of an organisation's workforce. However, it believes that the Bill as currently drafted is consistent with the key policy objectives underpinning the MySuper reforms: 'a simple, cost-effective default product...limited to a common set of features to make it easier for members, employers and other stakeholders to compare performance across MySuper products'. These features will encourage competition among MySuper product providers to lower fees."<sup>10</sup>*

The inference is that the MySuper regime is adequate but that the benefits of the new regime can only be fully realised by members where MySuper operates in an open and competitive market that forces issuers to compete on price, other product features and service. CFS agrees with this contention and foresees a truly open and competitive default market achieving the best outcomes for members.

## **CFS Recommendation**

The Government remove the ability of modern awards to specify default funds, allowing employers the freedom to select an APRA approved MySuper default fund based on their own consideration of the merits of each fund and what is in the best interests of members.

Yours sincerely,

Brian Bissaker  
CEO Colonial First State

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<sup>9</sup> Parliamentary Joint Committee on Corporations and Financial Services, Report on MySuper Core Provisions Bill 2011 and Trustee Obligations and Prudential Standards Bill 2012 p.61, March 2012

<sup>10</sup> Parliamentary Joint Committee on Corporations and Financial Services, Report on MySuper Core Provisions Bill 2011 and Trustee Obligations and Prudential Standards Bill 2012 p.39, March 2012