



Submission – Response to the Super System Review –
Phase 2

CHOICE

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1. Executive Summary

This document is a submission from CHOICE to Phase 2 of the *Super System Review* (the Cooper Review)..

CHOICE welcomes the opportunity to make an input to the reform of the Australian superannuation system. In this submission CHOICE has focussed on a small number of key areas where reform is most needed.

These issues are:

- Increasing the amount and quality of comparative data available to consumers;
- Removing the bias that results from sales commissions to advisers when recommending a superannuation fund to consumers;
- Introducing measures to decrease excessive fees and charges, including a new ‘fee target’ of 1%; and
- Introducing measures to reduce the number and impact of inactive and lost accounts.

In addition, CHOICE has provided answers to many of the specific questions raised in the Phase 2 Issues Paper. However, we are concerned that the proposed approach to reform outlined in the Issues Paper includes a large number of small reforms that may consume energy and resources to implement, and may not have a significant impact. CHOICE would prefer the Government to pursue a smaller number of reforms which are likely to have a significant impact.

2. About CHOICE

CHOICE is a leading advocate of consumer rights in Australia. As the public face of the Australian Consumers’ Association (ACA), CHOICE is a self funded body that is committed to providing consumers with advocacy and advice.

CHOICE has a long history of consumer advocacy in financial services and superannuation. In recent years CHOICE has campaigned for:

- An improved Consumer compensation scheme for financial services (October 2008);
- Improved options for the consolidation of Superannuation Accounts (November 2008); and
- The restructure of remuneration for financial advisers (July 2009).

3. Need for an independent voice for superannuation members

The superannuation system is complex, and is the subject of constant changes through Government reforms, technology and new product features. However, the interests of superannuation members (consumers) are not represented by a specialist consumer organisation or service.

Consumer representative organisations operate effectively in consumer credit, energy and communications, with a mix of community and government support.

There have been requests made to the Government to fund the establishment of a Superannuation Consumer Service for over fifteen years. The current review considered this issue briefly in the *Phase 1 Issues Paper*, but it is not mentioned in the *Preliminary Report*.

CHOICE submits that the complex issues raised in the *Phase 2 Issues Paper* are an excellent example of the issues and reforms that would benefit from a dedicated, independent consumer voice in superannuation. This new organisation would be free from the industry conflicts of interest that may arise for other associations and interest groups that currently operate in the sector.

The proposed organisation could replicate the successful advocacy and assistance model that is used by other organisations such as the Consumer Action Law Centre, the Australian Communications Consumer Action Network and many other independent consumer organisations. Under this model the organisation could provide a direct advice and assistance service to consumers, and use the information and lessons from this service to influence policy advocacy.

4. The key objectives of superannuation

Before turning to the detailed questions in the *Phase 2 Issues Paper*, it is important to comment on the key objectives of the superannuation system in Australia.

While recognising that superannuation serves several useful purposes in the Australian economy, CHOICE believes that the core objective of the superannuation system is to encourage and develop adequate income for retirement for individual consumers. Other secondary objectives, such as creating a large pool of potential funding for investments and infrastructure, should never become the primary drivers for superannuation policy.

5. Efficiency

CHOICE notes that although the basic pillars of Australia's superannuation are in place, the individual superannuation accounts held by Australians are not yet large enough for the industry to be considered 'mature'. Many superannuation balances remain small, because coverage was not universal until recently. Also, the absence of choice for many consumers prior to 2005 has resulted in a fragmented system and a high proportion of multiple accounts. Some industry analysts have noted that the system will not truly mature until 2030 or later, when the majority of the population will have account balances that reflect at least the full SGC, and the number of accounts will normalise at 1-2 per person.

As the system is not yet mature, some allowance can be made for inefficiencies in the system. While it is important to pursue efficiency gains, it should be recognised that some gains may require long term structural change. Proposals for short term fixes should be considered with great care.

CHOICE has identified some areas where efficiency gains could be pursued:

1. Facilitating competition to drive down costs (through greater transparency and comparability of fees, possibly complimented by fee targets); [discussed in section 9.3]
2. Reducing leakage (through measures to reduce the number of inactive and lost accounts and through measures to manage small account balances); [discussed in section 6.4]
3. Increasing account consolidation; [discussed in section 6.4]
4. Encouraging automated processing , e-commerce solutions and clearing houses [discussed in section 6.1]; and
5. Increasing standardisation [discussed in sections 6.2 and 8.1]

CHOICE also notes that some inefficiencies derive from marketing and sales practices. For example, the provision of numerous competing investment options, and the poor standard of advice provided by some planners and advisers who are heavily influenced by commissions.

CHOICE also notes that there has been some discussion of high-level inefficiencies in the superannuation industry through the prevalence of small and medium sized funds. Indeed, the Review has already considered mechanisms to reduce the number of funds and to encourage fund consolidation. While CHOICE agrees that there may be too many funds in the sector at the current time, CHOICE cautions that the consolidation of funds may not achieve all of the efficiencies that are predicted. There are numerous other industries where consolidation of providers has not resulted in efficiencies for consumers (e.g. banking and transport). CHOICE supports some limited measures to encourage consolidation of providers, but would prefer to see the majority of effort focus on consolidation of accounts.

6. Design / Architecture

[From this section on, the CHOICE submission follows the numbering in the Phase 2 Issues Paper]

6.1. Technology

6.1.1 Quantum leap

Could the Australian superannuation system use technology more to improve efficiencies and deliver lower costs? Is there a technological quantum leap for the super system to make...?

CHOICE believes that it may be unhelpful to expect a quantum leap in technology in the superannuation industry. It is more realistic to look at a few key technology and e-commerce initiatives that can deliver improvements for consumers.

The most likely candidate is the development of one or more 'clearing houses' for employers faced with the difficult task of making multiple SGC payments. This will have flow on benefits for consumers and may lead to a renewed interest in choice of fund.

CHOICE is concerned that some employers are resistant to employees (especially new employees) exercising choice of fund, because of the paperwork and administration hassle in making payments to multiple funds. While employers may technically comply with the choice of fund legislation, there are numerous subtle ways that an employee can be made to feel uncomfortable about exercising choice against the wishes of their employer.

6.1.2 Do super funds need to provide daily unit pricing?

Does it add extra expense if funds unit price daily or allow switching on every normal business day?
Would it reduce costs if this were to occur on a fortnightly (or other) basis in superannuation?

CHOICE submits that small reforms of this nature are unlikely to make a significant impact, and we would prefer the Review to concentrate on a smaller number of more significant reforms.

6.1.3 Data standards

Would some form of Government intervention to set rules and impose data standards over the various payment routes in the superannuation system assist stakeholders to improve efficiencies and deliver lower costs?

CHOICE agrees that improved data standardisation is needed, and would have benefits for consumers. However, we are aware of numerous existing and proposed industry initiatives regarding data standards. It appears that this issue is already being addressed.

We provide additional comments on data standards in Sections 6.2 and 8.1.

6.2. Default funds and default investment options

6.2.1 Employer selection of default fund

How do employers select a default fund? Is there a more effective and efficient method for selection of a default fund? Should there be a small number of default funds (or even a single default fund) to reduce costs and to take advantage of economies of scale (eg a Government-operated national default fund)?

CHOICE notes that there are a number of ways in which default funds are selected. Some default funds are chosen by negotiation (e.g. as part of the industry award). Others are simply determined by the employer acting alone (with or without advice).

It is essential that the overall standard of default funds is lifted, as many consumers are not actively exercising choice.

In the first instance, attempts should be made to lift the standard of default funds. Options could include:

- Mandating new (higher) standards for default funds;
- Requiring employers to consider and compare at least one non-profit fund during their selection of default funds;
- Further measures to prohibit kick-backs and other forms of influence for employers by default funds, including increased investigation, enforcement and penalties.

The proposed government Default Fund is of interest to consumer stakeholders. However, this proposal may over-complicate the system and deliver little benefit when compared to a system where the standards for default funds were working well (and were effectively enforced).

A compromise may be to develop a **small** panel of default funds, similar to the small panel of Eligible Rollover Funds (ERFs), which all meet high standards. The panel could be made available to employers through the new clearing house systems being developed. (However, it may still be necessary to allow some employers to select a different default fund where the selection resulted from group negotiation with employees, e.g. through industry awards).

6.2.2 A national default fund

Would a Government-operated national default fund be attractive to many small businesses and their employees, particularly if it were simply designed, low-cost and easy to understand? Should Australia have something similar to the national fund that is being introduced into the UK in 2012?

CHOICE believes that if the initiatives discussed in 6.2.1 (higher standards and a small panel of default funds) were pursued, the need for a new Government default fund may diminish. A new Government operated default fund is likely to be complex and expensive, and adds another layer to the complexity of superannuation. CHOICE is also concerned that it may not be appropriate to establish a Government owned competitor in an industry where some funds (especially non-profit funds) are already delivering affordable and high quality accounts for consumers.

However, if other initiatives fail, and concerns regarding default funds continue, this option could be reconsidered.

6.2.3 The typical Australian default investment option

Is it appropriate that the typical default investment option treats all members as having the same investment horizons and risk appetite? Should a lifecycle fund, or some similar model, be mandated as a default investment option?

CHOICE believes that it is important for default investment options to follow best practice, especially as many consumers are passive superannuation investors and are unlikely to exercise investment choices themselves.

However, CHOICE is also concerned that mandating specific lifecycle investment options may constrain investment managers and reduce flexibility during periods of high market volatility. For example, severe restrictions on the proportion of funds that can be invested in a particular asset category can have disastrous consequences for individual investors where they result in a forced asset sale or acquisition at exactly the wrong time in the market.

A better approach may be to require managers to disclose the default investment options as a targets range and allow some flexibility. Traditionally default investment options in Australia have had a slight bias towards growth assets in all lifecycle stages, and this is probably a reasonable approach for long term retirement incomes.

CHOICE is also concerned that some special issues are beginning to emerge for particular groups in Australia. Most default investment options are calculated on age. However, some demographic groups have very short life expectancy, e.g. indigenous consumers. CHOICE would support measures to accommodate the special needs of such groups.

CHOICE also notes that default investments options should always be trumped by individual requests. Even if individual requests tend to be overly conservative, members may have a reason for selecting defensive options, and freedom of choice regarding investment options should be allowed.

6.2.4 Design of default investment option

Should there be a prescribed asset allocation of the default investment option and more consistent labelling of all investment options? Is the current way in which default asset allocation decisions are made by trustees appropriate for members who don't make a choice? Should the default investment option in a default fund be substantially passively invested? Should the Government mandate certain features of default funds (eg investment strategy, fees etc)? Could APRA be empowered to give greater guidance?

CHOICE agrees with the proposal for more consistent labelling of default options. It is essential that consumer stakeholders are able to participate in any working group developing these new labels (this is another example of the need for an independent consumer voice for superannuation members).

Some current investment option labels have been the cause of considerable consumer misunderstanding and complaints, such as 'cash' and 'cash plus'. Not surprisingly, consumers are surprised to see that investments carrying these labels can lose value. The use of the term 'plus' appears to be widely misunderstood. To investment managers it means the freedom to invest in some additional assets. To consumers it may mean added protection. There are many other example of labelling problems.

Greater guidance and consistency on investment option labels is supported by CHOICE.

At this time, we do not support mandatory asset allocations. We note that flexibility in asset allocations has allowed new, innovative products (such as ethical investment options) to emerge.

6.2.5 Range of investment options

Should there be a statutory limit on the number of investment options that default funds can offer? What are the lessons arising from the GFC on the availability and design of investment options in super?

CHOICE does not support a limit on the number of investment options offered by funds.

The lessons from the GFC regarding investment options are complex. Some key lessons include:

- There is considerable consumer confusion over investment option labels, such as 'cash', 'cash plus' and 'defensive';
- Consumers have a limited understanding of the pros and cons of holding overseas assets (volatility, spreading risk, significant currency fluctuations);
- 'Balanced' and 'diversified' funds probably did not perform to the expectations of consumers, who believed they had some level of protection through spreading risk across multiple asset categories; and
- The process of 'reserving' and 'smoothing' by some funds is inconsistent and is not well understood by consumers, who expected a greater level of 'smoothing' during the GFC (based on many years of positive returns in the lead up to the crisis).

6.2.6 'Stickiness'

Are the current settings around how quickly members can change investment options or to leave the fund optimal? Would it be better for the system overall if member choices could only be implemented over longer periods than currently apply? ... Have super funds adequately embraced the opportunities available in infrastructure projects and other long-term unlisted investments?

The majority of Australian superannuation members are incredibly passive, and they are unlikely to exercise rapid choice or mobility options. The current choice and mobility options should be retained, to encourage greater participation by members.

This may have some theoretical impact on 'stickiness', but CHOICE cautions against any expectation that Australian superannuation funds should become major players in infrastructure investments. It is difficult for superannuation funds to take on the role of infrastructure managers. There may be conflicts with multiple other objectives (e.g. environmental sustainability v commercial exploitation), and infrastructure projects are often subject to Government control, subsidy and other forms of intervention. The skills and expertise of participants in the superannuation industry do not automatically translate to the skills and expertise needed to manage long-term infrastructure projects.

CHOICE would prefer to see superannuation funds concentrating on quality financial management and services to members.

6.3. Regulation

6.3.1 Effectiveness of regulation

Can the cost-effectiveness and usefulness of regulation in super be assessed? Should regulation in super be regularly reviewed to determine whether it continues to be appropriate and to achieve the purpose for which it was established? How could this be done?

Regulatory change should be a low priority in this Review – the superannuation system needs a period of stable regulation to develop knowledge and skills of regulators. The regulatory structure has been the subject of constant change for the last ten years and participants require a break from reform fatigue.

However, we support the transfer of the Superannuation Complaints Tribunal functions to the Financial Ombudsman Service [discussed in section 11.1].

6.3.2 Regulator efficiency

APRA and ASIC reviewed their administrative practices to identify unnecessary regulatory burdens that could be addressed. APRA and ASIC have also established a joint forum to provide industry with an opportunity to raise issues with regulatory coordination. Are there any other areas where the operations of these two regulators could be made more efficient?

Given the links between super contributions, the SGC, tax deductibility of certain individual contributions and the Government co-contribution, would there be advantage in having the ATO as the sole agency responsible for monitoring all super contributions?

The ATO should not be the sole agency with oversight of superannuation contributions. It is important to have ASIC and APRA involved, and working together, as they have a broader view of the entire financial services sector. The GFC has shown the importance of coordinated regulation in financial services.

6.4. Inactive Accounts, Lost Members and Eligible Rollover Funds

6.4.2 Optimal vehicles

Given their purpose, is there any reason to have more than one ERF nationally? Is the current configuration of ERFs optimal for ridding funds of lost or inactive/uneconomic members, but at the same time maximising the retirement savings of those whose benefits are, for one reason or another, in an ERF?

Consumer stakeholders expect some natural consolidation in the number of ERFs to occur over time, without the need for Government intervention. CHOICE would prefer to see energy directed to avoiding lost and inactive accounts, rather than directing energy and resources to the development of a single ERF.

6.4.3 Government role

Should the Government provide a single, low-cost ERF as a default for all lost or inactive/uneconomic member benefits?

There should be no further government role in ERFs at this time. Other improvements in the management of lost and inactive accounts should be allowed to work through the system for a period before reconsidering this issue.

6.4.4 Need for ERFs

Is the fact that there are so many lost or inactive/uneconomic accounts symptomatic of other problems that need addressing, rather than establishing a more efficient ERF to put them in? Is it a case of creating different incentives for trustees? Would a tax on super funds that had a higher than benchmark level of lost accounts make a difference or simply impose an added burden on active members? Have some sectors already been burdened with a membership demographic more predisposed to becoming lost or inactive? ... Is there a role for automatic consolidation of accounts via use of TFNs? Should each member be provided with a personal superannuation identification number that must be given to the trustee of each super fund in which the person participates during their working life (in the same way that employees must provide TFNs to employers)?

The Phase 2 Issues Paper notes that ERFs are expensive in percentage terms (although they are inexpensive in dollar terms). However, some of this data may be historical as it includes temporary resident superannuation accounts which will now be treated differently.

Very small accounts (less than \$200) will also now be forwarded to consolidated revenue so this will also help reduce the number of accounts in ERFs. (CHOICE notes that a better use of these 'swept up' funds would be for the money to be utilised to fund education, consumer representation, or even to act as a reserve for smoothing volatility).

CHOICE believes that it is essential that the TFN is used to help manage lost and inactive accounts. CHOICE is willing to act as a trusted party and to facilitate discussions between privacy and consumer advocates that we believe will result in removal of opposition to the use of TFNs as an identifier in superannuation. This would have a significant impact on lost and multiple accounts, with benefits for all stakeholders. It may also reduce the overall administration and costs of the superannuation industry. However, it is also important that this change is achieved through a trusted and consultative process. CHOICE believes this is one of the highest priority issues in superannuation reform.

CHOICE notes that there is unlikely to be any support for a new superannuation identifier or superannuation number. Such proposals regularly fail in Australia, where the introduction of national identifiers is widely opposed by the community.

7. Participants

7.1. Members

Possibly one of the biggest inefficiencies for members, even active members, is having multiple member accounts. It is generally not in a member's financial interests to have more than one account in the accumulation phase of an APRA-regulated fund. However, the average employee had approximately three accounts as at 30 June 2008.²⁶ Rice Warner has estimated that around \$333 million in fees were charged on 8 million unnecessary inactive member accounts (not including ERFs) in the year to 30 June 2008. This is a considerable wastage of potential retirement savings.

CHOICE agrees that the number of multiple member accounts is unacceptably high, and is causing inefficiencies for individual consumers and the superannuation system as a whole.

CHOICE commissioned research on this issue in 2008 and developed a detailed policy position, outlining measures that may assist in the prevent and consolidation of multiple accounts. See: <http://www.choice.com.au/Consumer-Action/Finance/Finance-policy-and-campaigns/Superannuation-accounts/Page/The-issue.aspx>

CHOICE supports the following measures to assist in the consolidation of multiple accounts:

- **Introduction of a superannuation clearing house for employers**
CHOICE supports this initiative and understands that the development of this clearing house is already a Government priority.
- **Allowing automatic consolidation of superannuation accounts**
CHOICE supports this proposal in principle. However, we believe that consumer representatives should be able to participate in the design of the process to consolidate accounts. We envisage that balances from inactive accounts can be consolidated into active accounts by a simple process of writing to the member, requiring them to 'do nothing' unless they object to the consolidation. In addition, we support consolidation of multiple lost and inactive accounts held in ERFs into a single ERF account, utilising the TFN as an identifier for this purpose. In both cases reasonable efforts should be made to identify and contact the consumer, but we accept that there is a need to keep such costs to a minimum.

7.2. Employers

While requiring more frequent contributions would potentially add to cash-flow issues for some employers, could there be sufficient administrative savings in aligning the frequency of payment of SG contributions with normal payroll activity to offset that?

CHOICE believes that this is not a vital change and it may be difficult to impose further conditions on employers in the current economic climate. The current payment frequency requirements appear sufficient.

7.2.1 The occupational model

Is it the most efficient model for employers to remain involved in superannuation management? Does the equal representation model for trustee boards and for policy committees of certain public offer funds add value or is there a better model? What do employers want from the super system?

The role of employers in superannuation management appears to be entirely unnecessary once funds are paid. While there are historical reasons for the participation of employers, there is no longer any reason for employers to have an ongoing management role in what is essentially a compulsory financial services product.

The role of employers in the management of superannuation funds is also weakened by choice of fund requirements and portability rules. It is no longer the case that all an employer's staff will belong to the same fund.

The requirement for equal trustees (employers and employees) should be phased out over time. However, it is important that the role of employees is maintained. Effective and fair management of superannuation requires a balance of professional experts and member representatives.

7.2.2 Accuracy of employee information

Should employers be under an obligation to supply better quality information about employees into the super system? Should the costs of a centralised exchange be spread across all fund members, including those in benefit payment phase, through an increase in the supervisory levy?

There is certainly a need for some improvement in the data standards used by employers and funds. However, CHOICE understands that there are substantial industry initiatives on these issues and further government intervention may be unnecessary. We do not support an additional levy to fund basic data standards.

This issue may also be addressed by the use of clearing houses and the potential use of the TFN to facilitate the identification of members.

7.2.3 Standard forms for super

Should there be a suite of standard forms across superannuation (eg member applications, making contributions, benefit payments, requesting a rollover) with standard terminology and standard information required? Should these be under APRA's control so that funds would have to use the forms approved by APRA from time to time? Would any other areas of administration benefit from standardisation?

CHOICE supports the development and use of standard forms, administered by APRA. This will improve portability and choice of fund. Some current funds do as much as possible to put barriers in the way of consumers attempting to exit their fund. Barriers include:

- Exit fees;
- Making exit forms difficult to find on the fund website (whereas entry forms are easy to find);
- Including a 'sales' page before an exit form can be accessed, listing all of the benefits of the current fund; and
- Including onerous requirements on exit forms for statutory declarations, documents to be witnessed by JPs etc. (no such requirements are included on entry forms).

Standard forms should avoid these requirements and encourage mobility.

CHOICE has strong concerns regarding the appropriateness of the current ATO form for superannuation choice of fund. The *Standard choice form* (NAT 13080) is available at:
<http://www.ato.gov.au/content/downloads/SPR56761NAT13080.pdf>

This form has acted as a barrier to choice and mobility, as it contains bureaucratic paperwork requirements that are almost impossible for consumers to fulfil. In particular, the form must be accompanied by "attachments" that satisfy the following criteria:

- a. a letter from the trustee stating that this is a complying fund or retirement savings account (RSA) or, for a self-managed superannuation fund, a copy of documentation from the Tax Office confirming the fund is regulated
- b. written evidence from the fund stating that they will accept contributions from my employer, and
- c. details about how my employer can make contributions to this fund.

In addition, the form asks for unnecessary details regarding the selected fund, such as the ABN and product identification number.

CHOICE notes that this form requires significant improvements so that the form does not act as yet another barrier to choice of fund and mobility. Key improvements are:

- Making the form shorter (it is 6 pages long);
- Using plain language;
- Remove the bureaucratic paperwork requirements; and
- Removing the requirement to provide any attachments.

7.2.4 Inducements from super funds or associates

Are there instances where super fund trustees or their associates provide discounts to employers on other products and services in order to influence the employer's selection of default fund? Is this practice prevalent and, if so, should section 68A of the SIS Act be strengthened?

CHOICE is very concerned about any form of inducement or kick-backs to employers. Consumer stakeholders have previously suggested that this issue could be balanced by a requirement for employers to offer at least one non-profit default fund to all employees, but this proposal was rejected.

We believe this proposal had considerable merit and should be re-considered.

7.2.5 Salary sacrifice

Under current rules, if an employee makes an effective salary sacrifice, the employer's SG contribution is required to be made only on the reduced salary amount. Does this discourage employees from salary sacrificing, particularly when the employer could be seen to benefit?

CHOICE agrees that this issue is a concern. Consumers are encouraged to salary sacrifice, yet they are unlikely to be aware that some employers reduce the SG amount in this way.

However, this issue may be more appropriate to consider in a review of comprehensive taxation arrangements (e.g. the Henry tax review). There may be unintended consequences if the Cooper Review makes one-off adjustments that have an impact on tax, without considering the comparative tax status of all investments and savings options.

7.2.6 Electronic funds transfer

Should it be mandatory for APRA-regulated funds to have an EFT facility so that payments can be made electronically? Would this be of help to employers who are currently forced to write cheques for a number of funds? If there are impediments or unacceptable costs preventing this from happening, what are they?

CHOICE supports efforts to eliminate cheques and move to an electronic system as the paperwork currently acts as a disincentive for Choice of Fund.

7.3. Investment Managers

As can be seen from the table (shown in issues paper), two-thirds of active managers did not perform better than the S&P/ASX 200 Accumulation Index for the five years to the end of 2008. Do trustees concentrate too heavily on strategies that rely on active trading of investments thereby incurring additional costs and taxes that ultimately reduce the returns to members? Should passive management styles play more of a role in super or is there a justification for using active managers widely?

While CHOICE shares concerns expressed in the Phase 2 Issues Paper regarding active management, it is unclear that there is any viable alternative. This is one area where it appears necessary to let the market determine whether an active or passive manager model is preferred.

7.4. Administrators

7.4.1 Administrators as systemically significant institutions

Are super fund administrators systemically significant institutions? Should there be minimum capital requirements and compulsory APRA licensing for super administrators, with accompanying operating standards? Alternatively, should APRA be empowered to engage directly with administrators, rather than through the relevant trustee as is currently the case?

CHOICE is concerned that this proposal seems to add an unnecessary level of regulation to the superannuation system. Trustees and investment managers should remain the key focus of regulation.

7.4.2 Disqualification

The SIS Act does not regulate administrators, though disclosure obligations (including whistle blowing), disqualification powers and enforcement provisions are applied to investment managers and custodians as well as trustees. Is this appropriate? Should the SIS Act be extended to administrators in this regard?

CHOICE is concerned that this proposal seems to add an unnecessary level of regulation to the superannuation system. Trustees and investment managers should remain the key focus of regulation.

7.4.3 Identity issues

What could be done to deliver a more foolproof low-cost means of verifying the identity of members, for example when they request a rollover to another fund, or to avoid multiple accounts that do not follow naming conventions? Should the current rules that make it difficult for members to switch and consolidate accounts (eg requiring certified copies of personal documents – Schedule 2A of the SIS Regulations) be relaxed?

CHOICE is willing to facilitate discussions with consumer and privacy advocates regarding potential use of the TFN to improve identity in super. [discussed in section 6.4.4]

CHOICE also supports relaxation of the requirement for certified copies of documents, noting that this acts as a barrier to portability, and that similar requirements are not in place for entry to superannuation.

7.4.4 Tax file numbers

As at February 2009, 92 per cent of statements reported on the ATO's member contribution statement system had a TFN. Under current Privacy Act guidelines, TFNs cannot be used by fund administrators to match against member accounts. Should this be changed so that TFNs can play a larger role in identifying member accounts? How could TFNs be made more robust - i.e. verifiable at the commencement of membership of a fund so various participants in the system could depend on the TFN being correct? Is there a privacy problem with using TFNs in this way when information about taxpayers and their ABNs is freely available?

CHOICE is willing to facilitate discussions with consumer and privacy advocates regarding potential use of the TFN to improve identity in super. Traditionally, privacy law has been a barrier to the use of the TFN for this purpose. However, there are opportunities to work closely with consumer and privacy advocates to overcome this barrier, by explaining the benefits of using the TFN to assist in the consolidation of lost and multiple accounts. It will be important to develop appropriate privacy rules and safeguards (again, in consultation with privacy and consumer organisations).

7.4.5 Pricing and performance fees

Does the downward pressure on administration fees risk making administration companies unviable in the long-term? Is this a concern for trustees? Would a 'user pays' system of administration be fairer to members and administrators so that those who make more demands on the administration system pay more?

Other stakeholders will be in a better position to address this issue. CHOICE has no comment at this stage.

7.5. The Value Chain

Refer to fees table in the issues paper. Are there any observations about fee levels across the component parts of each industry segment that would assist the work of the Review?

Are there any invisible costs that are not evident in fees data commonly used by the industry? If so, what are some examples and how could they be captured? In the retail sector, is there a trend for distribution (including wraps and platforms) to be gaining a larger share of fees? If so, why?

Other stakeholders will be in a better position to address this issue. CHOICE has no comment at this stage.

8. Information

8.1. Performance Data And Other Comparative Information

8.1.1 Data collection agency

Should APRA remain the sole collector and publisher of official superannuation data? Or should some or all of the data or functions be shared with other official collection agencies such as the Australian Bureau of Statistics?

Other stakeholders will be in a better position to address this issue. CHOICE has no comment at this stage.

8.1.2 Data scope

APRA is already collecting critical data in relation to prudential supervision. Should the scope of data collected be extended to include sub-fund data as well as other areas (yet to be identified)?

Other stakeholders will be in a better position to address this issue. CHOICE has no comment at this stage.

8.1.3 Investment returns

Is the investment performance data about super funds currently published by APRA adequate? APRA uses rate of return to measure fund investment performance. Is this the most appropriate fund performance metric? There has been debate on the need for APRA to publish investment returns for individual investment options within super funds. Should APRA persist in trying to identify an investment option that is comparable across all super funds? Would it assist consumers and policy-makers if there were standardised definitions of asset classes and investment options used in super funds

CHOICE notes that there are limitations in the whole of fund data that is collected and published by APRA. However, it is important that some reliable independent comparative data is published to counter advertising claims made by funds and claims made by advisers. This is definitely an area where there could be improvements in the standardisation and comparability of data.

8.1.4 Industry metrics and ratios

Are there other tools used by the industry to measure the relative costs and performance of super funds (i.e. efficiency)? Are existing metrics adequate for members, analysts and regulators?

Other stakeholders will be in a better position to address this issue. CHOICE has no comment at this stage.

8.1.5 After-tax reporting

Should any trustee be allowed to engage a fund manager to manage a portfolio or be remunerated for performance or report investment returns, other than on an after-tax basis? What impediments (if any) are there to an industry standard on after-tax reporting of investment returns?

CHOICE submits that it is important to have like for like comparisons available for consumers in the superannuation sector. We therefore support a mandatory requirement for all reporting to be on an 'after tax' basis, to aid comparability. It is also very important that work is undertaken to improve the standardisation and comparability of key industry terms such as 'cash' 'defensive' and 'capital guaranteed'.

8.2. Information Given to Members

8.2.1 Product Disclosure Statement

Should a default fund have a different PDS requirement from a fund that is actively chosen? Could super trustees be given the option of lodging a PDS with regulators, rather than automatically providing one to each new member? Would optional PDSs make more sense if there were fewer choices in super?

CHOICE submits that it is important not to over-complicate regulatory requirements regarding the role and availability of a PDS. There should be a standard approach (it is too complex to have different rules for default funds and selected funds). Also CHOICE notes the need for consistency with other similar financial services products, such as life insurance, so that consumers have the same expectations of the kind of information contained within a PDS.

Many PDSs are now emailed and not always printed, so the environmental impact of the PDS has also been reduced.

8.2.2 Advice to members

What is the most cost effective way to get advice to consumers? Should the Government subsidise advice in super?

It is important to note that the provision of advice in relation to superannuation is not always necessary and has often acted to the disadvantage of consumers, resulting in commission driven sales that push consumers towards expensive retail funds.

In contrast, advice does not play a significant role in non-profit industry funds yet they have millions of members. There is still a role for general advertising and media commentary in fund selection.

For those consumers who believe they require advice, it would be useful if they had the option to approach an independent, non-profit provider. This might require enhancing current services provided by some Government and community organisations, such as Centrelink and the National Information Centre on Retirement Investments (NICRI). Both these organisations focus on advice at the time of retirement, or close to retirement.

This means that there is a significant gap in the availability of non-profit, independent advice services for people entering superannuation or reviewing their superannuation options during the accumulation period. CHOICE submits that existing services should be enhanced, and these should be complemented by a new, specialist organisation representing the interests of superannuation members, with the ability to provide independent advice and assistance.

Where advice is provided by commercial advisers, and it results in churning, advisers should be subject to scrutiny regarding their commissions and any other source of influence or bias regarding their recommended fund.

Ideally, commissions and remuneration that results in a sales bias should be prohibited. Alternatively, advisers should be required to provide a detailed explanation of the reasons for churning a customer, that can withstand an objective assessment (e.g. by an independent EDR service).

8.2.3 Uniform fees and charges disclosure

Is there a way of boiling fees and charges down to a small number of distinct types (using mandated naming conventions) so that members could make useful comparisons between funds?

Would it be feasible to prohibit trustees from allowing any other fee or cost to be paid from the fund that did not fall within one of the four types, all of which would be fully disclosed using only the mandated nomenclature? Alternatively, could ASIC's enhanced fee disclosure regime be improved in any way to help members understand and compare fees between funds? Could the ACCC's component pricing policy be applied so that funds would have to provide a prominent single total price for the product offered?

CHOICE submits that an important first step in managing fees and charges is to *reduce* the number and complexity of fees. CHOICE believes that both exit and entry fees should be banned, as these act as a disincentive to mobility and they over-complicate fee comparisons. We note that entry and exit fees are charged in addition to buy / sell spreads on both entry and exit, effectively resulting in double-dipping for funds each time a member moves.

In addition, CHOICE believes that all administration fees should be combined into a single, comparable cost for consumers (e.g. a dollars per week figure). This will allow consumers to compare the administration costs of funds when making their fund and investment choices.

Asset fees must also be comparable, but some care needs to be taken here. It is unlikely that an ACCC style component pricing approach will work effectively in superannuation, as some funds charge differential fees based on the size of the account balance (e.g. 1.5% on the first \$100,000, followed by 0.75% on the remainder). Giving ASIC a greater role in fee disclosure may have benefits, as ASIC is trusted by multiple stakeholders and has gained useful experience on fee disclosure from other sectors of the financial system.

CHOICE notes that there is no consumer interest in seeing particular 'buckets' of costs or a complex break-down of costs. There is also little use in seeing average fees if they do not reflect reality.

Transparency requires much greater consistency regarding whether costs are disclosed pre-tax or after-tax, and there should be no ability to hide fees in the disclosure of asset growth / losses.

8.2.4 Government website dedicated to superannuation

Is there a role for a high-quality Government website solely dedicated to providing information about superannuation (possibly in other languages as well)? Could this assist in making disclosure cheaper and easier for trustees by allowing them to link to such a site, rather than having to reproduce 'boilerplate' information about super such as: preservation ages, taxation arrangements and so on in a wide range of different documents?

CHOICE supports this proposal, although we note there may be some overlap with the role of APRA in providing comparative data (current) and standard forms (proposed). Consumer representatives should have input into the site objectives, usability and content of the website if this proposal proceeds.

8.2.5 Traffic lights

Would it be feasible to require all funds to display on their websites and disclosure documents a simple traffic light symbol or some other easy to understand graphic, intended to highlight how the fund compared against its peers on fees and charges?

CHOICE supports the provision of easy to understand comparative data on investment returns, fees and overall costs. The traffic light proposal is of interest, but it may be very difficult to achieve, especially as some funds reduce fees for high balance customers.

8.2.6 Disclosure more generally

Are there more efficient ways that super funds could satisfy their various disclosure obligations? Alternatively, could super funds very cheaply and simply exceed those obligations by, for example, placing the fund's trust deed and other material agreements on the fund's website?

Some simplification of disclosure requirements is acceptable to consumer stakeholders, as savings may flow on to members. It is understandable that there is limited interest in detailed ongoing disclosure requirements by consumers in a 40 year compulsory product.

8.2.7 Annual reports

Are annual reports useful to members or could they be phased out with the information made available on the fund's website or another internet site?

Amendments in March 2009 to the Corporations Regulations make permanent the relief previously provided by ASIC allowing trustees to make the annual report available on their websites, rather than sending each member a printed copy. This is subject to requirements such as getting member approval and notifying members when the annual report is placed on the website.

CHOICE agrees that printed reports are no longer required. There is also some interest in the environmental impact of sending out printed reports. However, we note that many funds use the Annual Report as a marketing tool for cross-selling other products, promoting fund consolidation, promoting voluntary contributions etc., so it is likely that printed reports will continue to be distributed for some time.

The ASIC relief requirement for 'member approval' (for not distributing a printed annual report) now appears unnecessary and may be acting as a barrier to the use of electronic versions.

8.2.8 Remuneration

Is there currently adequate disclosure to members about the level of remuneration paid to directors and executives of super funds and about the remuneration arrangements of service providers (eg should members be able to find out about the incentive arrangements applicable to the executives of their investment managers)? Should the remuneration standards applied by APRA in relation to banks and insurers also apply to superannuation?

CHOICE believes that it is important for members to have access to this information - it may encourage greater involvement by members in the management of the fund.

8.2.9 Electronic communications generally

Is there room for further liberalisation of the extent to which trustees can communicate with members electronically? Could members who opt to receive paper communications, be required to pay for it?

CHOICE notes that it is important not to disadvantage those consumers who do not have access to affordable electronic services. However, we support the fullest possible liberalisation of electronic communication in the superannuation sector so that electronic options are at least available. We note that environmental concerns are now prominent in relation to unnecessary paperwork and postage.

8.2.10 Research houses

Are super fund members adequately served by the research on super funds generally available?

Other stakeholders will be in a better position to address this issue. CHOICE has no comment at this stage.

8.2.11 Calculators

Are online calculators helpful in allowing members to experiment with different scenarios for their super or is the quality of assumptions and other features still in need of some form of standards either via an industry code or more regulation?

CHOICE submits that small reforms of this nature are unlikely to make a significant impact, and we would prefer the Review to concentrate on a smaller number of more significant reforms.

8.2.12 Audited accounts

Would it assist analysts, advisers and some members if the fully audited accounts of all APRA-regulated super funds were required to be displayed on the fund's website, with hard copies available free of charge to members on request? Would it be more efficient if the accounts were in XBRL41 format so they could be more effectively interrogated and compared?

CHOICE submits that small reforms of this nature are unlikely to make a significant impact, and we would prefer the Review to concentrate on a smaller number of more significant reforms.

8.2.13 Renewal notices in super

What if, each year, funds were required to send members a bill for next year's estimated fees; effectively a renewal notice similar to those sent by insurers? What would be the practical implications of such a proposal? There would be an initial implementation cost and some ongoing administration cost, but would it drive greater efficiency in the long term?

CHOICE submits that renewal notices would be complex and expensive and the benefit is uncertain. We would prefer the Review to concentrate on other reforms.

9. Direct Costs

9.1. Fee Data

CHOICE is grateful for the fee data supplied in the Phase 2 Issues Paper. However, we question the constant categorisation of funds as either wholesale or retail, with industry funds appearing in the 'wholesale' category. A better form of categorisation may be to divide funds into for-profit and non-profit funds, and then have sub-categories within each division.

9.2. What do Commissions Cost Members?

CHOICE is grateful for the commission data supplied in the Phase 2 Issues Paper. More information on the breakdown of commissions would be useful (for example, the prevalence of commissions within different categories of funds).

9.3. Fees and Charges

9.3.1 Should there be a ceiling on fees in super?

Is there a basis for controlling fees in super in Australia, whether universally or in respect of members in default funds and default investment options? Whether on all contributions or just SG contributions? Should any controls be by regulation or by suasion and much improved fee information and disclosure?

CHOICE is concerned that the high level of fees in some retail funds is eroding the retirement incomes of Australians. There is also no clear link between the fees paid and the returns provided.

CHOICE expects that there will be a gradual reduction in average fees through competition, e-commerce, and other initiatives to tackle small, lost and inactive accounts. However, we are concerned that these changes may not deliver reduced fees for all members, and that these reductions will 'peter out' without further intervention.

CHOICE recognises that there may not be a 'silver bullet' solution available to this issue. There is some support for efforts to ensure that default funds are affordable, however CHOICE believes that *all* funds should be affordable.

We encourage the Government to consider addressing the high level of fees by setting a 'fee target' where the combined administration fee and asset fee should be no greater than 1%. This target should be subject to ongoing (downward) review.

CHOICE is willing to consider allowing fees above the target in exceptional circumstances. These might include:

- Allowing an extra fee to meet the specific requirements of a complex investment option, actively chosen by the member (e.g. charging a higher fee for an ethical investment option to reflect the extra work required to assess and select appropriate assets).
- Allowing an extra fee where the fee relates only to out-performance of the investment option against an agreed market benchmark (e.g. charging an additional fee as a percentage of the performance of the investment in those years when the investment outperformed an agreed index).

CHOICE also recognises that it may take some funds a moderate period to meet the fee target. For example, there may need to be greater alignment with the maturity of superannuation accounts in some funds, and some funds have a disproportionate number of small and inactive accounts.

In summary, we believe that a 'fee target' should be set by Government, that it should generally act as a mandatory ceiling on fees, with some exceptions for specific investment options, and some temporary exceptions or transitional arrangements for funds who cannot immediately meet the target. These arrangements will require the industry to work closely with regulators and other stakeholders to ensure appropriate governance.

CHOICE believes that the initial fee target should be 1%, subject to ongoing (downward) reviews.

A major concern for CHOICE is that the majority of current fees represent ‘money for nothing’. A significant proportion of Australian superannuation balances are invested in passive, mainstream assets, such as cash and stable blue chip shares. These are assets that could be held directly by members themselves at NO cost, but instead they are required to pay an asset management fee (and possibly other fees and commissions) simply because the assets are held in a superannuation vehicle.

It is also important to note that percentage based fees are a proportion of compulsory investments by members and will *naturally* grow each year for providers without any effort on their part. It is therefore essential for fees to be subject to downward pressure from somewhere (in this case the Government fee target), as there is very little pressure from the market.

CHOICE notes that the superannuation industry arguments in relation to fees are often couched in terms of the quality of service and advice, but there is no evidence of this delivering benefits to consumers. Even in the most expensive funds, consumers have a very disinterested and disconnected relationship with the fund, and their engagement is generally passive. There is also no evidence that consumers in expensive retail funds receive better service or get access to a wider range of products than consumers in low cost non-profit funds.

As noted in section 8.2.3, CHOICE also believe that some fee categories – entry and exit fees – should be completely removed. This will simplify cost comparisons and may improve downward pressure on fees through encouraging mobility.

9.3.2 Factory gate pricing

Factory gate pricing is where the cost of acquiring an interest in the fund is disclosed separately from fees relating to additional services like advice. This would see prices perhaps broken into: the basic product (which would include the investment management fee), a separate administration fee and a separately priced advice component. Members could then decide whether they wanted advice and, if so, how much, rather than just being presented with a bundled price. Would factory gate pricing help in super?

It is difficult to understand this argument – advice should always be optional and the price of advice should always be disclosed as a separate item. If this is not currently the case then CHOICE would be interested in further discussion of this issue.

9.3.3 Commissions on employer contributions

Should trustees be allowed to pay trailing commissions in respect of employer SG contributions or, more correctly, should trustees be allowed to increase fees charged in respect of employer contributions in order to fund trailing commissions payable to advisers? Should the position be different in respect of members of default funds, or default investment options within default funds where, on the face of it, no marketing or distribution costs are involved and little or no advice is given?

CHOICE believes there should be no distinction between default and selected funds – it is important to be consistent about this and to encourage simplicity. Trailing commissions are not supported by consumer representatives, and these should be banned. It is very unfortunate if trail commissions are eating into compulsory SGC contributions.

We also note that ongoing remuneration for advice paid out of member’s funds is not a question for trustees but for members. It should not be allowed unless express consumer consent is given on an individual basis for advice services. Consent cannot be given in perpetuity but should be renegotiated / reconfirmed at least annually.

9.3.4 'Shelf-space' fees

Are shelf fees an unnecessary layer of complexity and cost to members and, if so, what should be done about them?

It is difficult to estimate the impact of shelf fees – they may not be a major issue. Other stakeholders will be in a better position to address this issue. CHOICE has no comment at this stage.

9.3.5 Exit fees

Exit fees (in addition to a sell spread) are sometimes charged by super funds when a member leaves the fund. Sometimes the fees expire after a period and sometimes not. The 2007 Parliamentary Joint Committee Inquiry into super recommended that exit fees in excess of the actual transaction costs of exiting the member be prohibited prospectively. Do you agree, or disagree, with this recommendation? If so, why?

CHOICE submits that exit fees should be completely banned. They act as a significant deterrent to choice of fund and mobility. Most funds also incorporate buy and sell spreads in their unit pricing, so exit fees represent double-dipping. Exit fees also complicate fee comparison across funds.

9.3.6 Buy spread

Is it necessary to charge a buy spread on all contributions to a super fund? Some funds do not charge any buy spread, but others do. Is this cost difficult for members to identify and understand? Is there a better way of distributing transaction costs equitably across the members? Should they be captured within the Indirect Cost Ratio calculations or just phased out of superannuation altogether?

Other stakeholders will be in a better position to address this issue. CHOICE has no comment at this stage.

9.3.7 'Flipping' members to personal plans

Should trustees be able, unilaterally, to move members out of an employer plan to a personal plan with higher fees, often coupled with less insurance, when a member changes jobs (i.e. cease to be employer-sponsored)?

CHOICE submits that consumers should be provided with a full range of information and the opportunity to select alternative funds before they are subject to an automatic transfer of this nature.

9.3.8 Placement agent fees

In this context, a placement agent refers to a person who locates capital for investment managers, generally by dealing with super funds and their asset consultants, in return for a commission payable by the investment manager. The cost of such commissions is then embedded in the price paid by the fund for the investment, correspondingly reducing the long-term return to members. Do placement agent fees have a place in super? Are special rules needed regarding the use of placement agents?

Other stakeholders will be in a better position to address this issue. CHOICE has no comment at this stage.

9.3.9 Interactions between super funds and life company statutory funds

Do investments by super funds in the statutory funds of related life companies lead to an obscuring of fees and costs charged while in that structure? What value is added to the superannuation fund by investing through a life office structure, rather than through other asset management devices?

Other stakeholders will be in a better position to address this issue. CHOICE has no comment at this stage.

9.3.10 Fees in a default fund

If a member is in a default fund, is it appropriate that the same level of fees and commissions are charged in respect of that member in contrast to a member who chose that fund on advice? Should there be limits on the fees and commissions that can be charged to default members in default funds (both at asset level and member account level)?

CHOICE believes there should be no distinction between default and selected funds in relation to fee arrangements – it is important to be consistent about this and to encourage simplicity. CHOICE does not support commissions on any superannuation or investment product.

9.4. Percentage Remuneration

Under an internal funds management model, scale benefits the member because the costs per member of running the fund are diluted as the fund grows in size and so fees per member can be reduced. Under the external model, fees reduce only if the manager agrees to cap them as scale increases and hence the manager generally reaps the reward from scale. What factors have played a part in the Australian industry adopting the external model? Would other models work in Australia?

Under the external model, there is a strong incentive to expand products and gather assets, rather than reduce costs or achieve operational efficiencies. Where the investment manager is an associate of the trustee, there might be a common duty to the parent entity to maximise operational profits, and this might be achieved by making pricing less than transparent to the member. Where this is the case, should the trustee be obliged to disclose expressly the profit expectations of the parent?

What is the best way to encourage trustees to strike the most appropriate balance between in-house and outsourced investment management to optimise returns to members?

CHOICE believes that fees should reduce in line with growth of the fund. If this is not being achieved by traditional market forces, then the proposed ‘fee target;’ approach outlined in section 9.3 may assist.

9.5. Potential to Simplify Fees by Eliminating Rebates

Is the current system of rebates driven, in part, by unit pricing considerations (i.e. the need to only have one price at fund level)?

CHOICE submits that fee rebates distort the overall costs to members, as well as resulting in complex disclosure to consumers and the unnecessary and circular transfer of money. Fee rebates are largely the by-product of the commission driven sales system, which is opposed by CHOICE.

Rather than eliminating rebates, the Review should be examining ways to eliminate commission driven sales. The requirement to treat all members equally may need to be revised to state that members will be treated fairly, so that differential fees can be charged for members with large balances. Over time this will benefit all members.

CHOICE also believes that the industry should be required to demonstrate that their fees are justified, and that their method of calculating fees bears some relationship to the costs incurred by the fund.

9.5.1 Cost and transparency

How much more does it cost to administer a system of rebates, rather than transparent discounts or mark-ups? Why are fees for additional services, like advice, not added to the price of the product as occurs in other industries?

CHOICE opposes commission driven sales and supports the simplification of pricing structures in superannuation.

9.6. Performance Fees

9.6.1 Standards

Should there be some form of standards applying to performance fees?

CHOICE supports an increased role for performance fees in superannuation as these provide a greater link between fees and the quality of investment management. Many other fees in superannuation represent a 'money for nothing' approach to remuneration. CHOICE submits that performance fees should meet the following criteria:

- Performance fees must be based on out-performance against an agreed benchmark;
- Performance fees should be based on medium to long-term periods, and should never be paid for short-interval gains (e.g. less than six months);
- Performance fees (like all fees) should be calculated and disclosed on an after-tax basis; and
- Performance fees should be considered an exception to the 'fee target' [discussed in section 9.3] and may therefore be subject to additional governance, oversight and standards to justify the exception.

Overall, we believe that performance fees may play a role in returning fairness to the relationship between members and investment managers. Fees based on a proportion of gains (above agreed benchmarks) appear more appropriate than fees charged as a simple proportion of assets, where the size of assets will grow through compulsory SGC contributions without any work by the investment manager.

9.6.2 Discount on other fees

Should performance-based fees only be allowed if there is a tangible discount in fixed fees, perhaps to a floor equivalent to the cost of the service or even less?

CHOICE submits that the size of other fees should be managed through the 'fee target' approach discussed in section 9.3.

9.6.3 Prohibition

Should performance fees be prohibited on assets invested in the default investment option and in ERFs?

CHOICE does not support increased complexity in the rules for default investment options and ERFs. Our preference is for consistency between all funds and all investment options regarding fees.

Instead, we propose that performance fees should be treated as a justifiable exception to the 'fee target' approach. They could be used in any fund and in any investment option, including default funds and ERFs.

9.7. Other Ways to Reduce Costs

Are there other areas where super funds could save money and, if so, what are they? Are there areas where too much money has already been saved, that is, are there areas where costs pressures have reduced services to the detriment or potential detriment of members?

Other stakeholders will be in a better position to address this issue. CHOICE has no comment at this stage.

10. Inefficient Behaviour

10.1. Clearer Statement of Beliefs and Objectives

Could it lead to better outcomes for members if trustees were required to explain clearly and on a regular basis what their investment beliefs were, the objectives of each investment option offered and the broad objectives of the fund itself?

CHOICE submits that small reforms of this nature are unlikely to make a significant impact, and we would prefer the Review to concentrate on a smaller number of more significant reforms.

CHOICE would, however, support a requirement for all funds to disclose clearly whether or not they are non-profit or for-profit organisations.

10.2. Costs in Prices and Spreads

Do trustees have the necessary tools and mechanisms to ensure that the members' best financial interests are adequately protected in relation to these issues?

Costs in prices and spreads are used by trustees to attempt to achieve fair outcomes for all members of the fund, so that the impact of members joining and leaving the fund does not have an unfair impact on the majority of members. Over time, all members should reap the benefit of these arrangements.

CHOICE supports the use of spreads to manage this issue, rather than the use of entry or exit fees. Entry and exit fees act as a disincentive to choice of fund and mobility, and they also complicate fee comparison. CHOICE submits that entry and exit fees should be banned.

10.3. Competition

10.3.1 Impact of choice of fund

Do the advantages of choice of fund outweigh the costs to members and employers? Could choice arrangements be varied so as to reduce deadweight costs in the system?

CHOICE supports choice of fund and believes that the benefits of offering choice of fund will be substantial over time. To date, the benefits have been muted, as there are still substantial barriers to exercising choice. However, we expect that a greater proportion of members will exercise choice in the future, if certain changes discussed elsewhere in this submission are implemented. These include:

- The introduction of clearing houses and e-commerce options, that will reduce employer disincentives relating to choice. We believe that some employers exercise subtle forms of persuasion against choice due to real and perceived administration hassles associated with making payments to multiple funds.
- Improved standardisation of fee and costs disclosure. This should send an improved price signal to consumers, providing an incentive to exercise choice.
- Removing entry and exit fees, as these serve as a barrier to exercising choice and also complicate fee comparisons.
- Standardising entry and exit forms and removing unnecessary requirements on exit forms that have served as a barrier to choice and mobility.
- Clearer disclosure of whether funds are for-profit or non-profit.

10.3.2 Bargaining power of trustees

Trustees of super funds seem to be price-takers in the market for investment management services. Is this the case and, if it is, what can be done to balance the power of trustees to strike more favourable prices for members?

Other stakeholders will be in a better position to address this issue. CHOICE has no comment at this stage.

10.3.3 Outsourcing model

As super funds get bigger, should they continue to outsource to such a large extent? ...Would it be more cost-effective for more services to be performed in-house?

Other stakeholders will be in a better position to address this issue. CHOICE has no comment at this stage.

10.3.4 Complexity and information asymmetry

There is evidence of consumers having significant difficulty understanding super. Does the complexity and information asymmetry in super make normal demand-led price competition difficult, if not impossible?

CHOICE agrees that consumers have difficult understanding some key concepts and terms used in superannuation products. Most of the complexity relates to the disclosure of fees and returns in a way which makes price comparison difficult for ordinary consumers.

Some measures regarding standardisation, simplification and improved disclosure are discussed elsewhere in this submission. In addition, consumers would benefit from a dedicated consumer organisation specialising in superannuation issues, to represent superannuation members in advocating for law reform, improvements in industry practice, and increased consumer awareness and literacy.

10.3.5 Sharing of infrastructure

Is there more room for the sharing of infrastructure or forming alliances in super to reduce costs? If so, what prevents it from happening currently?

Other stakeholders will be in a better position to address this issue. CHOICE has no comment at this stage.

10.4. The Cost of Short-Termism

10.4.1 Excessive focus on short-term returns

Is it appropriate that trustees of super funds concern themselves with 'peer risk' and hence make decisions that are focused on short-term returns? Does the focus on matching peer performance reduce genuine differentiation between superannuation funds and hence make the capacity to choose between funds less meaningful? Does daily unit pricing drive short-termism?

Short termism is a difficult issue to address. It is true that superannuation has become a market linked product and performance is monitored in the same way that other financial services (including very short term products) are monitored. This form of comparison may tend to create a short term bias.

However, it is difficult to propose a workable alternative. Even if the disclosure of returns was heavily regulated to encourage long-term assessments (e.g. requiring funds to only disclose 5 and 10 year average returns), it is likely that intermediaries and media outlets would still disclose short-term returns, and these would continue to be compared with other short term products (e.g. term deposits).

CHOICE submits that this issue will be difficult to address, and energy and resources may be better directed to other proposals in the Phase 2 Issues Paper.

10.4.2 All things to all members?

Is there currently a trend for many super funds to seek to be 'all things to all members', offering a wide range of choices and services in order to keep up with perceived risks from competitors who offer them? Or are these wide ranges of choice and services because of member demand? Can the cost of this trend be estimated? Is there an argument that this level of choice is unnecessary?

The Phase 2 Issues Paper appears overly concerned with the number and cost of multiple products currently available to consumers. Consumer stakeholders have noted the detrimental impact of product and provider consolidation in other sectors, and would caution against any moves to artificially restrict the number of products at this stage.

10.5. Achieving Economies of Scale?

Have there been impediments to the further consolidation of super funds in Australia? If so, what are they?

The Review is interested in observations from trustees that have been involved in fund growth by merger and successor fund transfers. Were economies of scale expected and were they achieved? If not, what were the impediments? Were there systems, legal/regulatory, cultural or other issues that prevented reductions in costs per member? Is there a size that has to be reached in the Australian market before economies of scale occur? If so, what is it?

CHOICE recognises that the current superannuation market includes a large number of small funds, who face challenges in achieving economies of scale. However, CHOICE cautions that the consolidation of funds may not achieve all of the efficiencies that are predicted. There are numerous other industries where consolidation of providers has not resulted in efficiencies for consumers (e.g. banking and transport).

CHOICE supports some limited measures to encourage consolidation of providers, but would prefer to see the majority of effort focus on consolidation of accounts. CHOICE does not support any artificial consolidation measures that would reduce competition or innovation in the superannuation sector. We note that the sector is not yet fully mature, and that average balances will grow steadily over the next twenty years. This natural growth should help funds to achieve economies of scale over time.

10.6. Innovation

Are there sufficient incentives in place for trustees (and other participants in the super industry) to pursue innovative measures to increase the efficiency of their operations or do the potential risks outweigh the advantages? Could the tax system be used to motivate a greater focus on efficiency? Are there examples of innovation in other industries that could be useful for the Australian superannuation industry?

CHOICE supports measures aimed at increasing innovation in the industry. It may be appropriate to develop rewards for innovation and research through research funding, awards, scholarships, grants schemes and other similar measures.

If a tax incentive is to be considered as a way of encouraging innovation, we note that this may be more appropriate to consider in a review of comprehensive taxation arrangements (e.g. the Henry tax review), in order to achieve consistency across industries.

11. Other

11.1. Miscellaneous Issues

11.1.1 Other systems

Do any other countries have systems for defined contributions funds that operate more efficiently and generate better outcomes for members in any particular respect than our system? What are the features of that system?

Other stakeholders are better positioned to answer this question. Consumer stakeholders have limited experience and expertise in issues affecting defined benefit funds.

11.1.2 Death benefits

Could current arrangements surrounding payment of death benefits be simplified to reduce the discretion of trustees, and hence remove a source of disputes within the industry? For example, would it be useful to mandate that, in the absence of a binding death benefit nomination, any death benefit would simply be paid to the deceased member's estate? Is the claim of creditors against the estate the main problem with automatic payment to the estate? Are there others? Should all nominations (unless clearly legally invalid) be binding? Are the interdependency rules helpful to trustees?

CHOICE agrees that this issue may benefit from a new, consistent approach. However, we caution against rushing into a decision to mandate binding nominations. Consumer stakeholders, regulators and EDR schemes have some experience in managing complaints and inquiries regarding the payment of death benefits. This issue should be considered by a multi-stakeholder working group and estate planning experts, who could develop a new, consistent guide or rules for industry on the payment of death benefits.

11.1.3 Grandfathering

Successive governments have sought to protect the interests of superannuation fund members from any adverse impact of change in the system by 'grandfathering' pre-existing entitlements. Over time, the number of people protected tends to decline, but all funds must maintain systems and procedures to accommodate those various entitlements. Is there any capacity to reduce the number of grandfathered provisions?

CHOICE is concerned that grandfathering pre-existing arrangements has led to a complex and fragmented system of managing superannuation accounts. CHOICE opposes any further grandfathering and submits that this practice should not be pursued for any of the reforms considered in the current Review.

11.1.4 Sole purpose test

Are super funds engaged in activities that cost members and consequently, should not be undertaken? Alternatively, should a more open approach apply to the sole purpose test so that funds could provide a range of other products to members? Is the sole purpose test in section 62 of the SIS Act: too restrictive or about right?

Are existing members' interests being protected where fund assets are spent on advertising and sponsorship? Could there be a justification for banning advertising by super funds? Should the sole purpose test be amended to address this issue specifically?

CHOICE submits that the sole purpose test is working well and should not be broadened. The sole purpose test should *not* be used as a tool to manage fees or performance (other tools are available, as discussed elsewhere in this submission).

CHOICE believes that a reasonable amount of advertising is necessary and acceptable in the superannuation industry, and that this is already accommodated within the current sole purpose test.

11.1.5 Horizontal equity

Should all defined contribution funds be required to be unitised and subject to more uniform, transparent and rigorous valuation and unit pricing rules? Alternatively, are crediting rates a better mechanism for super?

Other stakeholders are better positioned to answer this question. Consumer stakeholders have limited experience and expertise in issues affecting defined benefit and defined contribution funds.

11.1.6 Harmonisation of benefit payment timeframes

The various timeframes for movement of superannuation money are inconsistent. For example, movement between investment options within a fund (no timeframe); out of a fund, but within the system (30 days for portability requests, 90 days for family law splits); out of the system (90 days for family law payments; 'as soon as practicable' for death and retirement benefits and on prescribed days for unclaimed temporary residents benefits). It seems that compliance with those timeframes is uneven across the system. What are possible solutions to this situation?

CHOICE would support a minor project aimed at harmonisation of time periods in the superannuation sector, although we do not consider this to be a major issue.

11.1.7 Member-protection for small accounts

A recent report cited a Rice Warner estimate that member protection costs industry super funds around ten basis points per annum in additional fees per member. Is member protection achieving its policy objective or acting as a disincentive to consolidate small accounts? Should it be retained? Would another solution be to reduce the services provided to small accounts (eg mail outs)?

CHOICE is concerned about the impact of member protection on the overall costs of superannuation. Consumer stakeholders may be willing to discuss the removal of member protection for small accounts, subject to conditions. This would need to be achieved through a trusted and consultative process. We believe that the future focus of regulation in this area should be on account consolidation rather than protecting small balances.

11.1.8 Should super be covered by the GEERS scheme?

The General Employee Entitlements and Redundancy Scheme (GEERS) is a Government scheme that helps former employees who are owed entitlements (eg unpaid wages, annual leave and redundancy pay) by bankrupt or externally administered employers. Unremitted employer contributions to super are not included in GEERS; should they be?

Other stakeholders will be in a better position to address this issue. CHOICE has no comment at this stage.

11.1.9 Dispute resolution

Does the Superannuation Complaints Tribunal have sufficiently wide powers to deal with complaints in super? Should the time limit on TPD claims be extended to 5 or 10 years or even eliminated altogether? Trustees currently have 90 days to respond to a complaint before a member can go to the Tribunal. Is this too long? Should it be shortened to, say, 45 days?

CHOICE has been a long term supporter of affordable EDR schemes in the financial services sector. In recent years, the number of EDR schemes in the sector has been reduced, resulting in the Financial Ombudsman Service (FOS) acting as a one-stop shop for consumer complaints.

CHOICE can see some benefits in the activities of the Superannuation Complaints Tribunal being rolled into the FOS. FOS has a higher profile than the SCT and a greater level of engagement with consumer stakeholder representatives.