

12 February 2014

Manager
Superannuation Unit
Financial System Division
The Treasury
Langton Crescent
PARKES ACT 2600

Email: superannuationconsultatin@treasury.gov.au

Subject: Better regulation and governance, enhanced transparency and improved competition in superannuation - *Enhancing competition in the default superannuation market*

Dear Sir/Madam,

Colonial First State (CFS) is one of Australia's largest wealth management organisations with over \$96 billion in funds under management and, as part of the Wealth Management division of the Commonwealth Bank Group, contributes to a retail market share of around 15.71%.¹ Our flagship platform, FirstChoice, is the largest investment platform in the Australian market with \$64 billion in funds under management and includes our retail corporate superannuation product, FirstChoice Employer Superannuation which operates in the default fund market. FirstChoice Employer Super has around \$7.7 billion in funds under administration and over 7,100 employer plans and 240,000 members.² CFS superannuation funds are not currently, and never have been, named in any modern award.

CFS has long been a market leader in platform pricing and service. Colonial First State was the first retail superannuation fund to receive a MySuper authorisation from APRA (through the FirstChoice Employer Super Fund). For employer plans of a certain size we offer our new MySuper product at a competitive fee of 0.80% and \$5 per month. Our platforms provide leading administrative speed and efficiency that means clients can transact today and receive a confirmation tomorrow. CFS's FirstChoice and FirstWrap have

¹ Plan for Life, administrator view, September 2013

² As at December 2013

been ranked No.1 and No. 2 respectively by financial advisers for overall satisfaction in the 2013 Wealth Insights Service Level Survey.³

Overview

CFS makes this submission solely to address our concerns about the current award default superannuation fund selection process given our strong belief that there is a need for policy change.

We thank the Government for its interest in this area of public policy and for its willingness to consult with the industry on possible ways to reform the relevant legislation to enhance competition in the default fund market. CFS has contributed to the Financial Services Council (FSC) submission on the Discussion Paper and we endorse that submission on this and the many other issues it addresses.

CFS has advocated on this issue for a number of years, through the Cooper Review and Stronger Super consultation process, the Productivity Commission Review, and the introduction of legislation in 2013 to amend the Fair Work Act. Throughout this period we have consistently argued for genuine and open competition and transparency in the default superannuation market by allowing any MySuper product to compete for the right to be an employer's default superannuation fund. We were disappointed at the overall legislative outcome reached in 2013 and we believe further legislative reform is necessary to improve competition, transparency, and to deregulate the superannuation default fund sector.

Recommendation – the law should be amended to remove the listing of default superannuation funds from modern awards, allowing employers to choose any MySuper product as a default fund for award employees.

The current default fund selection process

CFS believes the process for the selection of default funds in awards imposes unnecessary cost and regulatory burden on funds. Funds are required to have an APRA-authorized MySuper product. However, they also need to apply to the Fair Work Commission's (FWC) Expert Panel to be included in the default superannuation fund list (First Stage) and apply to the Full bench of the Fair Work Commission to be listed in each modern award in which they seek to be named (Second Stage).

It is conceivable that some, if not many, superannuation funds would seek to be named on all 122 modern awards. This is especially the case for funds such as ours, with many existing employer plans across multiple industries and employers. These employers require our fund to be listed in order to be able to continue to make compulsory super contributions to the fund on behalf of their employees.

³ Wealth Insights 2013 Platform Service level Report and survey of 859 aligned and non-aligned financial advisers Feb/Mar 2013

Trustees have only recently undertaken the costly, lengthy and rigorous process of achieving APRA MySuper product authorisation. For them to now have to apply to another body for the right to compete to provide services to a significant segment of the market is duplicative, onerous, and imposes unnecessary extra cost.

We note the FSC, in its submission, has indicated the approximate compliance costs involved in the fund application process.

Why should any MySuper product be able to be selected by employers as a default fund?

With the introduction of MySuper the regulatory requirements for default superannuation products have increased substantially to ensure default members could rely on a safe retirement savings vehicle. To quote the former Minister, *"MySuper will provide a simple, cost-effective default product that all Australians can rely on."*⁴

There are a range of safeguards attached to MySuper products which allow employers to feel safe and secure when selecting a MySuper product as their default fund. These include:

- The APRA authorisation process - all MySuper products must pass through the fine filter of APRA approval, ensuring they meet the relevant standards. APRA are effectively the gatekeeper of the 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, price competitive products – all MySuper products are required to meet strict standards with respect to fees, investment strategies, insurance settings and other services.
- Higher trustee duties – all trustees who offer a MySuper product have increased duties and obligations over and above those applicable to trustees operating solely in the superannuation choice sector.
- The scale requirement – all MySuper trustees are required to determine whether the fund has sufficient scale to continue to act in the best interests of members.

Most MySuper products have been released onto the market in recent months. In our view it would be imprudent to require them to pass different or higher hurdles before regulators, industry and government have had the opportunity to observe the operation and performance of these safeguards over a period of time.

Apart from the increased regulatory burden trustees will face there may be other unintended and negative consequences on the default fund market as a result of the introduction of the FWC's extra quality filter, such as:

- Undermining public confidence in MySuper – if only certain MySuper funds are appropriate for selection in Modern Awards, arguably, those

⁴ The Hon. Bill Shorten MP, Minister for Financial Services and Superannuation, House of Representatives Hansard, 3 November 2011, pp.12683-12684

- MySuper funds that are not appropriate could be considered flawed or inferior. Indeed, the rationale for MySuper itself could be questioned;
- Undermining APRA's role – a significant element of the Government's Stronger Super reforms is APRA's role in the creation and ongoing monitoring of trustee obligations and standards, including those applicable to MySuper. In demanding separate criteria, the FWC process may potentially erode APRA's role in ensuring all default members receive adequate protections; and
 - A failure to address existing competition issues in the default market by creating a two-tiered system.

Given the concerns raised above our strong preference is not to impose a further quality filter over and above the existing MySuper requirements.

Recommendation – any MySuper product should be able to be selected by an employer as their default superannuation fund for award employees.

Impact on existing employers

During the previous industrial award reform process (2008-09) the former Government inserted clauses into modern awards to grandfather existing default superannuation fund arrangements. Under this grandfathering, employers contributing to existing superannuation funds (before 20 September 2008) could continue making contributions into that fund even though the fund was not a named fund in a modern award. Under *Fair Work Act* amendments passed in 2013, these grandfathering provisions were removed. However, irrespective of the existence of grandfathering, under the current framework employers have no certainty that their existing fund (even those currently named in awards) will be named in the relevant award once the FWC process is complete.

To the extent that an employer's current default fund is not named in a modern award, from 1 January 2015 the employer will be required to make default contributions to a new fund. For employers and employee/members alike this will create unnecessary disruption and is likely to result in extra costs, inefficiencies and poor outcomes for consumers. For example, employees will have multiple accounts in different funds, two insurance policies and there is the real possibility that members could move to a fund paying higher fees than in their existing fund.

We recognise that, outside of the standard listing process, an employer can apply to a specific existing corporate or tailored MySuper plan listed separately by the FWC. The advantage of this process is that it is not limited by a number of funds per award. CFS's FirstChoice Employer Superannuation (FCES) primarily targets smaller employer plans and is not a corporate fund. It therefore cannot access this separate process. Unless FCES is named on at least a majority of award default fund lists we fear significant disruption for the many thousands of small employers we service.

Recommendation – existing default fund arrangements should be grandfathered.

Existing FWC process - Timing

Given its previous statements on this matter we believe there is some likelihood the Government will respond to this Discussion Paper by reforming the existing model. However, the FWC is required to continue to implement the new regime for the selection of default funds in accordance with the legislation (as amended in 2013) and irrespective of the Government's policy announcements. Indeed it has already begun this work and there is now every chance that the FWC will determine new default listings by 1 January 2015, in time for new default contributions to be made to those funds on behalf of award employees.

If the Government chooses to reform the current framework there is no indication of when these reforms would commence. Further, this may be determined by factors such as the ease and speed with which the Parliament would agree to pass such reforms. In the event that the FWC completes all modern award default fund listings by 1 January 2015, yet government reforms are not operational until sometime after, employers may be prohibited from contributing to funds that they had previously selected as their default fund. They may also be prohibited from contributing to funds they had otherwise wished to continue using. Complicating matters further, employers may soon after be permitted to contribute to that preferred fund once again as a result of changes introduced by the Government.

To require employers to pay contributions into a different fund for this short period of time would be a dislocating and inefficient outcome. To ensure this is avoided we suggest the deadline for contributions to be paid into new listed default funds be extended from 1 January 2015 to 1 July 2015. This will also allow employers sufficient time to become educated about, and transition to, the new model. We understand the FWC could effect such a deferral through future determinations.

Recommendation – the Government should request the FWC make determinations to amend awards delaying the requirement for default contributions to be paid into named MySuper products until 1 July 2015.

Existing FWC Process - Standing

We look forward to the Government considering industry submissions for reform to the FWC process for the selection of default funds and potentially adopting our recommendations. From a business planning perspective CFS would like to assume this outcome with certainty. However, given the timing and grandfathering issues explained above we have no choice but to apply for our funds to be listed in the modern awards.

We take this opportunity to make a brief comment on the existing FWC process. We observe that superannuation funds do not have standing to make submissions and be heard before the Full Bench of the FWC as part of the Second Stage. This is disappointing. CFS is not a registered organisation and therefore cannot make submissions in the Second Stage. We note there will be a number of funds in other sectors which benefit not only from their position of incumbency but also as a result of being owned by, or having a close association with, certain registered organisations.

There is a clear competitive issue to be resolved in this regard. We believe competition will be enhanced by giving superannuation funds, which have successfully passed the First Stage, the right to make direct submissions to the FWC as part of the Second Stage.

Recommendation – to ensure a level playing field in relation to the default fund application process superannuation funds should be afforded standing to make submissions as part of the Second Stage.

We would be happy to discuss any aspect of this submission with you. Please contact Nicolette Rubinsztein (General Manager, Retirement and Advocacy) on [REDACTED] in the first instance if you have any questions relating to the content of this submission.

Yours faithfully,

A handwritten signature in black ink, appearing to read 'L Elkins', with a stylized flourish at the end.

Linda Elkins
Executive General Manager
Colonial First State