SUPER SYSTEM REVIEW
FINAL REPORT

PART ONE

Overview and Recommendations

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30 June 2010

The Hon Chris Bowen MP
Minister for Financial Services, Superannuation and Corporate Law
Parliament House
CANBERRA ACT 2600

Dear Minister

Review of the Governance, Efficiency, Structure and Operation of Australia's Superannuation System

We are pleased to present the final report of the Super System Review.

We have developed ten recommendation packages aimed at benefiting members.

MySuper sits at the heart of our recommendations. It is designed to focus funds on the core purpose for which they exist: optimising retirement incomes for members.

SuperStream is a recognition that bringing the back office of super into the 21st century is critical to the overall functioning of the super system.

We are confident that all of our recommendations will enhance Australia's world class retirement savings system and we commend them to you.

Yours sincerely

Jeremy Cooper
Chair

Kevin Casey

Greg Evans

Sandy Grant

David Gruen

Meg Heffron

Ian Martin

Brian Wilson

TERMS OF REFERENCE

The then Minister for Superannuation and Corporate Law, Senator the Hon Nick Sherry, announced the Super System Review (**Review**) on 29 May 2009.[1] The Review was initiated with the support of the superannuation industry.[2] The terms of reference are as follows:

Review into the governance, efficiency, structure and operation of Australia's superannuation system.

Scope

1. The Review will comprehensively examine and analyse the governance, efficiency, structure and operation of Australia's superannuation system, including both compulsory and voluntary aspects, addressing, but not limited to, the following issues:

   1.1 Governance: examining the legal and regulatory framework of the superannuation system, including issues of trustee knowledge, skills and training; and thoroughly assess the risks involved in the use of debt and leverage and the development of investment options that lead to a weakening of the diversification principle in the superannuation system;

   1.2 Efficiency: ensuring the most efficient operation of the superannuation system for all members, whether active or passive members and whether making compulsory or voluntary contributions, including removing unnecessary complexities from the system and ensuring, in light of its compulsory nature, that it operates in the most cost effective manner and in the best interests of members;

   1.3 Structure: promoting effective competition in the superannuation system that leads to downward pressure on system costs, examining current add-on features of the superannuation system; and, examining other structural legacy features of the system; and

   1.4 Operation: maximising returns to members, including through minimising costs, covering both passive defaulting members, who should receive maximum returns and value for money through soundly regulated default products, and active selecting members, who should not be negatively impacted by conflicts of interest that may inhibit advice being in the best interests of members.

2. The Review to be conducted around the concepts of the best interests of the member and the maximising of retirement incomes for Australians.

3. The Review to be conducted with reference to improving the regulation of the superannuation system, whilst also reducing business costs within the system.

4. The Review will be a systemic examination, including all superannuation fund sectors.

5. In conducting its work, and in determining its recommendations, the Review will have regard to the Communiqué of Principles (see separate attachment to this release).

6. The Review will comparatively examine international jurisdictions and will consult with experts as needed from other jurisdictions.

7. The Review is excluded from considering the issues before the Australia's Future Tax System review concerning system inputs such as the level of superannuation contributions, taxation including taxation concessions and other incentives.

8. The Review is excluded from considering the development of a superannuation clearing house or the project addressing the consolidation of lost accounts, as these are the subject of separate and already commenced processes.

Composition and Consultation

9. The Review to be led by an expert panel made up of a full-time Chair and five[3] part-time members, supported by a secretariat drawing on the skills of the key policy and regulatory agencies of the Commonwealth, as well as market expertise. The Review may also draw on external expertise where necessary.

10. The Review will consult the superannuation industry, other stakeholders and the broader public.

Timing

11. The Review will make recommendations to the Government by 30 June 2010 on possible options for reform, including appropriate transitional arrangements. The Review may report on particular issues prior to the finalisation of the final report.

CONTENTS

1 REVIEW HIGHLIGHTS

1.1 Engagement

Australians have contributions made to their super funds whether they like it or not. Members should not have to be interested, financially literate, or investment experts to get the most out of their super. If members want to engage and make choices, then the system ought to encourage and facilitate them doing so. If members are not interested, then the system should still work to provide optimal outcomes for them. The super system should work for its members, not vice versa. This is the basis of the Panel's new 'choice architecture'.

1.2 MySuper

MySuper is a simple, well-designed product suitable for the majority of members. The MySuper concept is aimed at lowering overall costs while maintaining a competitive market-based, private sector infrastructure for super. The concept draws on and enhances an existing and well-known product (the default investment option). MySuper takes this product, simplifies it, adds scale, transparency and comparability, all aimed at achieving better member outcomes.

1.3 SuperStream

SuperStream is a package of measures designed to bring the back-office of superannuation into the 21st century. Its key components are the increased use of technology, uniform data standards, use of the tax file number as a key identifier and the straight-through processing of superannuation transactions.

1.4 Regulating for efficiency

APRA would have an increased mandate to oversee and promote the overall efficiency and transparency of the superannuation system. To this end, APRA would be given a standards-making power in superannuation as a tool for driving transparency and comparability of member outcomes.

1.5 SMSFs

The SMSF sector is largely successful and well-functioning. Significant changes are not required, but measures relating to service providers, auditors and the regulatory framework are recommended.

1.6 Scale matters

There are substantial benefits for members arising out of increased scale in the superannuation industry. MySuper providers would be exposed to scrutiny and pressure on this issue and would be required to consider each year whether they had sufficient scale to optimise outcomes for members.

1.7 Governance

Nearly all the issues looked at in the Review link back to trustee governance in some way or other. Improving governance practices and structures is key to improving member outcomes. A Code of Trustee Governance is proposed.

1.8 Helping members compare

In order to make meaningful choices (or to understand their personal situation) members need to be able to make 'like with like' comparisons between competing superannuation products. Standard product 'dashboards' and standardised investment performance reporting would lift the fog that has clouded this area so far.

1.9 Insurance in super

Commissions should be banned on all insurance products in super, including group risk and personal insurance. Trustees will continue to be able to offer life, TPD and income protection insurance in MySuper and choice investment options.

1.10 Systemic transparency

Each fund would be required to provide free of charge on its website, detailed financial and operational information about the fund (including its portfolio holdings) and about the fund's management to greatly increase accountability and availability of information to those who are interested.

1.11 Whole of life focus

The super system exists to enhance retirement incomes for working Australians, not simply to accumulate assets. MySuper should be a whole of life product and include a single type of retirement income stream product chosen by the trustee and not just cater for members in the pre-retirement phase. Trustees would have a duty to address longevity, inflation and investment risks for retirement phase members in developing their strategies.

1.12 Data

Improving the quality and availability of data and research on the superannuation industry facilitates decision-making, ensures participants in the industry are held to account by members, regulators and peers and gives confidence in the integrity of the system. The importance of this issue justifies regulatory intervention so APRA would have an increased role in this area.

1.13 Dollar savings for the system

Treasury estimates short-term annual system savings of about $1.55B and long term annual system savings of around $2.7B as a result of MySuper and SuperStream.

1.14 Dollar savings for members

Treasury estimates that the MySuper and SuperStream proposals would, in the long-run, see a cut of around 40 per cent in fees for the average member. This would lift their final superannuation balance by around $40,000 or 7 per cent after 37 years in the work force.

About this final report

This final report supersedes all of the Panel's preliminary reports. The final report of the Super System Review comprises the following:

- **Part One:** Overview of the Review, including a consolidated list of all the Panel's recommendations and a summary of how they impact members; and

- **Part Two:** The Panel's 10 recommendation packages, each in its own chapter.

2 THE PANEL'S 10 SUPER POLICY PRINCIPLES

The Panel recognises the wider government policy concerns that affect the superannuation system: overall fiscal sustainability, broader retirement policy and taxation policy among them. However, in shaping its recommendations, the Panel has formulated 10 principles about superannuation, which have underpinned its decision-making process.

The Panel believes that these principles have broader application than just this Review. They should be the guiding principles by which policy is developed in relation to superannuation generally, to ensure consistency of approach to superannuation policy by successive Australian governments.

1. Superannuation must always be for the benefit of members. The superannuation system does not exist to support intermediaries. Trustees must be relentless in seeking benefits for members.

2. The superannuation system needs to be well-regulated to address prudential and other risks so that members can have the confidence to invest their retirement savings for their long-term financial benefit.

3. Transparency and disclosure are essential for the effective operation of the system, but are not substitutes for well-designed products that work in members' interests. Disclosure is a necessary, but not a sufficient, condition for ensuring that member interests prevail.

4. Individual choices for members should be available and respected, but members must recognise and accept the increased responsibility that comes with making those choices.

5. The superannuation system must be supported by high quality research and data, as well as by intermediaries with high professional standards.

6. Financial literacy is an important long term goal, but a compulsory superannuation system cannot depend on all its participants having the skills necessary to comprehend complex financial information or being investment experts.

7. Fees and costs matter; they detract from members' retirement savings and need to be managed as diligently as the generation of investment returns. Technological improvements, and innovation generally, should be encouraged to help lower costs and benefit members.

8. Superannuation is a large and complex system with an increasingly important social and macroeconomic dimension. It must be regulated and administered coherently and rule changes, including to taxation rules, should be made sparingly and in a way that engenders member confidence.

9. The system must have sufficient flexibility to accommodate its inherent growth path and should strive for continual improvement, rather than abrupt changes. Where possible, government and trustee decisions about superannuation should be taken with a long-term perspective.

10. Governments should not seek to direct super fund trustees to invest in particular assets or asset classes, nor to prevent investments in certain types of assets or asset classes unless there are prudential or regulatory reasons for doing so. This is regardless of how much it might seem in the national interest to do so.

3 THE CASE FOR REFORM

3.1 The superannuation system in 2035

Australians have over a trillion dollars[4] in superannuation savings.[5] The compulsory nature of super contributions means that by 2035, Australians are projected to have increased their collective super savings to $6.1T.[6]

This Review provides a valuable opportunity to take stock of the current system in light of how it might develop and to make recommendations designed to enhance its simplicity, efficiency and equity.

Just as in 1993, when the current architecture of the system was established, it is hard to envisage exactly the course those changes will take. In 1993, total superannuation assets amounted to $183B,[7] and the industry was dominated by corporate funds and by large, partly-funded public sector schemes. The SMSF sector, as we know it today, did not exist.

For an overview of the superannuation system today, see appendix B.

Forecasting the size and structure of the superannuation system over the coming 25 years is not an easy task, given the system's dynamism and complexity. However, Treasury projections show a quite dramatic decrease in the number of funds so that the large APRA fund sector is dominated by fewer, larger super funds.

Table 1: The Australian superannuation industry in 2035 (including SMSFs)

	1996	June 2009	2035 (nominal)[8]	2035 (current)
Overall industry scale	$245b	$1.1t	$6.1t	$3.2t
Ratio of accumulation to post-retirement assets	-	4:1	3:1	3:1
Biggest fund	-	$41.5b	$350b	$187b
Number of large APRA funds (excluding ERFs)	4734	447	74	74
Average large APRA fund size	$40m	$1.5b	$53b	$28b
Average accumulation member balance	$15,000	$70,000	$335,000	$180,000
Total super assets - proportion of GDP	**47%**	**90%**	**130%**	**130%**

3.2 The key challenges

The projected figures in table 1 are based on Treasury modelling and are subject to a number of assumptions (explained in appendix C). They do, however, throw into sharp relief the sorts of issues that the Panel believes that government and community need to be thinking about and addressing now, to position the super system to respond the challenges of the future.

3.2.1 Issues for the future

Funds will be much larger: The average fund will be much larger in real (2010 dollar) terms. This, in turn, will have implications for fund governance, for investment and prudential regulation. The largest funds will be very large by current standards, though even they will remain relatively modest by global standards.

Asset-based fees will grow: Asset-based fees will grow with the size of the asset pool and will require continued vigilance to ensure that total dollar fee levels remain appropriate, rather than merely focusing on percentages not increasing or trending slightly downwards.

Member account balances will be larger: Member account balances will be substantially larger in real terms, than at any time in the history of superannuation. This will put pressure on member transfer and remediation processes across the system and will increase concerns around identity theft and fraud and trustee accountability to members. It might also encourage greater member engagement as superannuation balances make a more material contribution to the retirement incomes of more Australians.

Economically significant: The superannuation system will continue to be an important factor in the Australian economy and financial markets. The efficiency of the sector will have macro-economic effects.

Competing in the global market place: Local funds will increasingly find themselves competing with large global funds, not just in markets for listed securities, but also for specific assets, such as infrastructure, private equity and direct property.

3.2.2 Issues that need to be addressed now

The future growth of the industry sets the current issues in their broader context and highlights the need for reform.

Member interests are not always paramount: Superannuation is compulsory and fully outsourced to the private sector. System design and regulatory settings have perhaps not taken this into account sufficiently. Member interests are not always paramount.

Immature system for its size: Overall, it is a system that has not yet reached a level of maturity commensurate with its monetary scale.

'Efficiency' is outside the regulatory net: The regulatory model has focused mainly on prudential safety which, while important, has left the efficiency of the system for members in the hands of market participants.

Too much complexity: Members perceive superannuation as too complex and opaque and there is an overall lack of transparency and comparability of superannuation products.

Disclosure to members has failed to achieve its objectives: Whatever the actual level of engagement and literacy among members, a regulatory model largely built around detailed disclosure and member choice has not worked for a substantial portion of the member population.

Ambiguity about trustee role when members make active choices: Where members do make choices about their superannuation in a large APRA fund, there is a lack of clarity about how much responsibility they are taking and how much the trustee is looking after them.

Past-performance data given too much prominence – sometimes at member expense: Much of the explicit and implicit marketing that occurs in superannuation is based on past investment return performance, often pre-tax and unaudited and almost always without reference to volatility.

Antiquated division of industry along 'retail' and 'industry' lines persists: The sectoral classifications such as 'industry' and 'retail' are redundant and in some cases obscure clear identification of the issues.

Inadequate accounting and financial reporting standards: The accounting and financial reporting standards applying to super are inadequate because they are directed to entity reporting; a perspective in which only a fraction of participants are interested.

Back office dominated by manual transactions: The back office of super is in urgent need of an upgrade and annually costs members hundreds of millions of dollars more than it should.

Lack of scale: Many funds lack the scale necessary to provide optimal outcomes to their members and, in some cases, trustee self-interest has hindered rationalisations that are clearly in members' interests.

Fees too high: Fees in superannuation have not reduced in line with what could have been expected given economies of scale that are clearly present or available.

Too much tinkering: The frequency of changes to rules about super can undermine member confidence in the system.

3.3 Why hasn't competition delivered optimal outcomes already?

In classical economic theory, markets efficiently allocate resources, shape products and determine prices. In superannuation, competition in the market for super at the consumer level (ie between funds competing for the business of a new member) has so far been relatively weak.

This is because superannuation is different. In addition to the fact that super is compulsory, normal consumer demand-led competition is made more difficult because:

Failure to exercise choice: Often a member doesn't choose the fund to which they belong. New employees typically simply become a member of their employer's default fund;

Lack of price awareness: Compulsory contributions don't come directly out of members' pockets, nor do the fees and other costs charged by the fund (at least not until they retire). This makes people much less price aware and much less likely to make a decision based on price or cost;

Lack of interest: Members are often not engaged with their super until closer to retirement and so will not be sufficiently interested to respond to competitive behaviour on the part of funds until that time (if at all);

Agency and structural issues: There are limited opportunities for member vigilance, on the one hand, or incentives for agency vigilance, on the other, to reduce prices;

Complexity: Super is inherently complex and many consumers do not feel confident making decisions about it;

Lack of comparability: Even if members are engaged up to a point, there is a lack of contestability at consumer level because of product complexity and lack of information and transparency about fees and performance; and

Frictions: Lastly, even if someone is interested in switching funds, often the paperwork and other 'frictions' in changing funds become too big a disincentive and they give up.

It has to be said that the original superannuation architecture was somewhat optimistic in that it relied on notions of market forces, disclosure and competition (along with trust concepts) to resolve consumer issues surrounding complex products, structures and conflicts.

The Panel therefore accepts that the model of member-driven competition through 'choice of fund' (in the form of SG Act choice and consequent portability) has struggled to deliver a competitive market that reduces costs for members.

The Panel also believes that the failure of competition to deliver desirable outcomes for members encapsulates the broader issue in the industry as it currently operates: it is remote from the member. The Panel recognised early on that, for real benefits to flow to members as a consequence of this Review, the superannuation system must operate from the member perspective.

4 THE SUPER FUND MEMBER

4.1 The theory of rational and informed investors vs real life experience

A key tenet of the 1997 Wallis Report was that super fund members should be treated as rational and informed investors, with disclosure and market conduct controls being the main regulatory instruments with which to oversee the industry.[9]

More specifically, these settings assume that members have the tools at their disposal, and the necessary regulatory protections in the market place, to enable them to make optimal decisions about their investment strategies, about when to enter and exit the market, and about what to do with their super on reaching retirement. In a compulsory system, it also assumes that members have the requisite degree of interest.

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

The 2006 Adult Literacy and Life Skills Survey of Australians published by the Australian Bureau of Statistics (**ABS**) in January 2008, found that 46 per cent of 15-74-year olds, or some seven million people, would struggle to understand documentation such as job applications, maps and payroll forms. Fifty-three per cent of surveyed Australians reached just the second of five levels in a practical numeracy test, while 70 per cent (about 10.6M people) managed only to progress to level 2 in a series of problem-solving exercises. Level 3 is regarded by the survey developers as the minimum required for individuals to meet the complex demands of everyday life and work in the emerging knowledge-based economy.[10]

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

4.2 Engagement with super

The financial literacy issues highlight one of the ongoing tensions and debates for this Review: what it means to be an 'engaged' super member and how 'engagement' should be pursued, facilitated or encouraged. The Panel's key concern has been the suggestion that a certain level of engagement and financial literacy is necessary for the system to work properly.

Since the introduction of the 'Choice of Super' legislation, switching rates between funds have actually declined from around 5 per cent in 2005 to 2 per cent by the end of 2009.[11] A Roy Morgan Research report, based on over 50,000 interviews conducted annually, indicates that approximately 80 per cent of super fund switches come as a result of members changing employers or employers changing default fund providers.[12]

Of those who default into a super fund chosen by their employer, or award, roughly 80 per cent are in the default investment option.[13] Of that 80 per cent, anecdotal evidence suggests that approximately 20 per cent of default investment option members do choose to be in the default investment option. This suggests that approximately 60 per cent of members do not make active choices.

However, the Panel is conscious not to overstate the level of member 'disengagement'. The Panel recognises that there are segments of the community very much engaged with their super and who spend time thinking and making active decisions about superannuation.

One thing is clear: the level of engagement of any individual member will depend on a range of factors, for example the member's age, account balance, and broader financial and life circumstances. The key point from the Panel's perspective is that a compulsory system needs to be able to cater for these different degrees of engagement: the significant proportion of members who are not engaged with their super, or in a position to make the sorts of decisions required of them; and the informed, financially literate, or well-advised members.

4.3 Philosophical framework of MySuper and the choice architecture model

These realisations about financial literacy and engagement have led the Panel to propose the new 'choice architecture' framework for the Australian superannuation system that is detailed in this report. This framework is an adaptation of contemporary thinking in the field of behavioural economics. This field is currently being applied overseas to a variety of complex public policy challenges involving consumers - for example, in the fields of health care, child nutrition, road safety and sustainability, as well as retirement savings.[14]

The key tenet of this approach is the concept of 'libertarian paternalism' – the idea that the outcomes experienced by inert or disengaged consumers should have inbuilt settings that most closely suit those consumers' objective needs, as assessed by the expert providers of the product or service in question.[15]

Importantly, this does not amount to a centrally-determined 'boilerplate' option for everybody, as it must at all times have regard to the collective characteristics of the particular consumers affected, any of whom can at any time opt out if they want to take more control for themselves. Nor is it a completely *laissez-faire* system of unimpeded choices where providers can be indifferent to the selection decisions made (or not made) by individuals. This is because the default setting must always be one that reflects a positive judgment about the most appropriate outcome for the consumer (member) in the eyes of the product provider (being the trustee in the case of a superannuation fund).

5 INTRODUCTION TO THE RECOMMENDATION PACKAGES

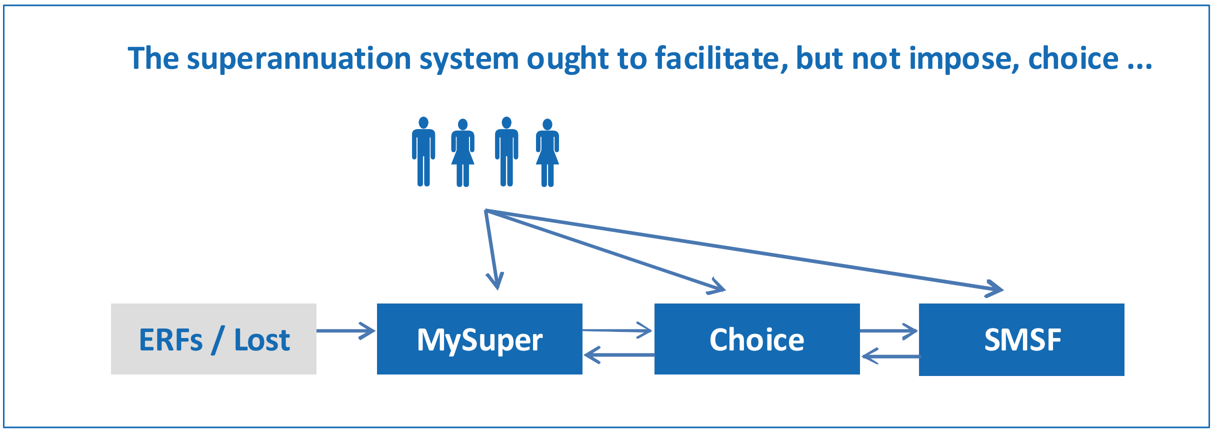
The Panel has framed its recommendations in 10 'packages', each being a chapter in Part Two of this report, making up a comprehensive blueprint for reform. Earlier versions of some of these packages have been released as preliminary reports during the course of the Review (see appendix A for a full listing of these preliminary reports).

Wherever possible, the Panel has pitched its recommendations, and its analysis, at what it regards as the key conceptual issues and not matters of legislative or operational detail. Given the time and resources available to it, the Panel necessarily had to refrain from engaging in a more granulated review of the complicated legislative and regulatory environment that has built up around the superannuation system.

5.1 Chapter 1: MySuper and the choice architecture

The Panel has re-cast the architecture of the superannuation industry to a member-oriented, rather than an industry-oriented, perspective. It believes that the system should facilitate, but not be based on, choice. That is, the degree of engagement a member wants to exercise in relation to their superannuation should dictate the regulatory settings and the nature of the products available.

Figure 1: A choice architecture model for Australia's superannuation system

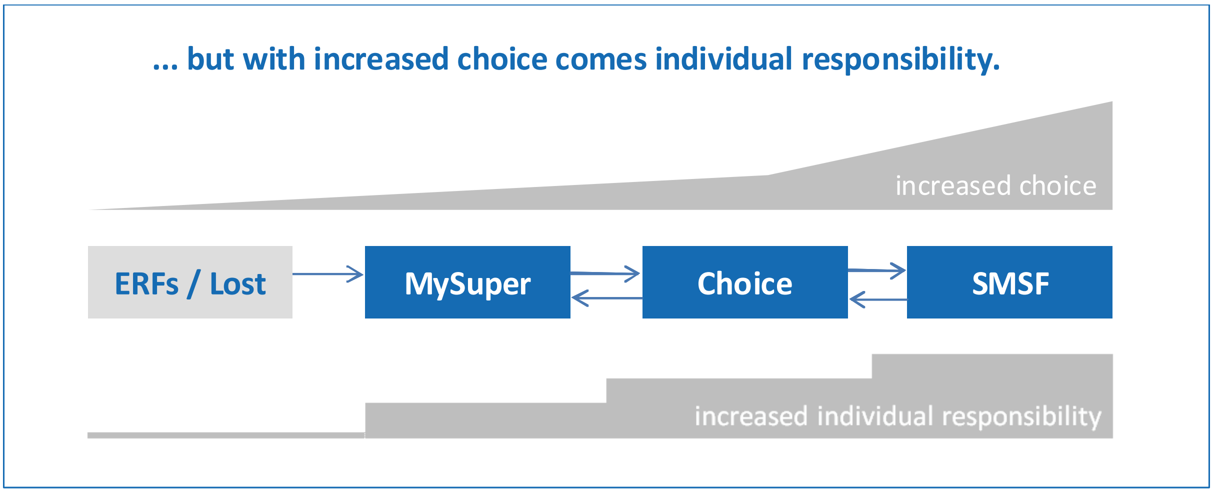


Broadly speaking, the architecture recognises four types of members.

- There are some members who simply want someone else to take care of it all for them. MySuper is particularly designed to cater to these members.
- There are some members who want to exercise choice over the investment strategies applied to their superannuation balances, but want to have their accounts administered for them. These members can elect to be in the choice segment, though they might decide that a MySuper product meets their needs and elect to have their money invested there (or in a combination of MySuper and choice products).
- There are some, and the number has increased sharply in recent years, who choose to be fully responsible for the investment and administration of their superannuation arrangements. These members can choose to operate an SMSF.

- The system also has to cater for members who have lost their superannuation account. The objective here is to reconnect members and their accounts quickly and efficiently and to introduce measures that make this less likely to occur in future.

Figure 2: Increased choice, increased member responsibility



5.1.1 MySuper

The MySuper component of the choice architecture model aims to provide a simple, cost effective product with a single, diversified portfolio of investments for the vast majority of Australian workers (roughly 80 per cent of members) who are in the default option in their current fund.

MySuper is designed with two large groups of members in mind: those who take no real interest in their super (at least not initially) and those who choose to be in a large, low-cost and well-managed product where the investment strategy is designed and implemented by the trustee.

MySuper would have a number of features designed solely with the member in mind: specific trustee duties designed to deliver lower cost outcomes for members; increased transparency leading to better comparability, especially of costs and long-term net performance; provision of intra-fund advice; simpler communications; and an embedded retirement product. It has been designed to sit within the existing superannuation structures and is based on existing widely offered and well understood default investment options.

5.1.2 Choice

The choice sector is also an important component of Australia's superannuation system. The Panel recognises that a competitive choice sector works well for members who want to tailor their superannuation.

But, even within choice, there are graduated degrees of member responsibility and engagement. While the Panel believes that the trustee should be protected when a member chooses a particular investment option that causes that member to suffer loss, the trustee also has a responsibility to apply a greater level of scrutiny to the sorts of products that are offered to super fund members in the master trusts, platforms or wrap environment. It should not be possible for trustees merely to preside over a menu of investment options principally selected by 'dealer groups' or other external parties.

Currently, the Australian financial services regulatory regime does not assess the suitability of products made available to retail investors, including members of certain types of super funds. Instead, disclosure is said to enable investors to decide for themselves what product is appropriate and neither APRA nor ASIC passes judgment on the merits or suitability of the investment.

This regulatory policy affects super because members are able to access a wide range of non-super financial products through master trusts, platforms and wraps (often many hundreds of products). This has resulted in some members sometimes choosing risky and illiquid investments that are arguably unsuitable as retirement products.

The Panel has recommend a refined duty on the part of a choice trustee to carry out appropriate due diligence and monitoring of investment options they offer. The details of this new duty would be fleshed out in standards to be developed by APRA in consultation with the industry.

5.2 Chapter 2: Trustee governance

The Panel believes that the combined effect of a compulsory system (outsourced by government to the private sector) and legislated preservation of benefits demand a higher level of governance in respect of super fund members than the level required for shareholders in major listed companies. Investors in listed companies have chosen to invest and are free to sell their holdings at any time.

The Panel has recommended several initiatives to improve trustee governance.

The Panel sees value in creating a distinct new office under statute, that of ‘trustee-director’. The duties, powers and standards required of this office would be recorded clearly in the SIS Act and nowhere else. These statutory duties would enhance, expand and clarify the duties set out in section 52(2) of the SIS Act as well as appropriately adapt the chapter 2D directors’ duties from the Corporations Act. The identification and management of conflicts of interests and of duties are a particular priority. Though conflicts are covered under the general law pertaining to trustees, it is clear from the Review’s analysis that there is a need for greater clarity of what is required of superannuation fund trustees and trustee-directors in this regard.

Changes are also required in relation to the structure of trustee boards, including their size and the tenure of trustee-directors. Contemporary best practice in corporate governance for listed companies includes the presence of independent directors on the board. The Panel believes that a minimum number of ‘non-associated’ trustee-directors (such that they can genuinely influence the decisions of those boards) should be required on all superannuation trustee boards.

To support the recommended legislative changes, the Panel proposes the establishment of a Code of Trustee Governance which would reflect the unique context of a superannuation fund. This Code would not be binding law and, as such, would be more flexible than legislation and could keep pace more easily with changes in the industry. This Code would be developed by industry.

As part of improving accountability to members, the Panel has recommended that a trustee should provide a member with reasons for its decisions in relation to a member’s formal complaint.

5.3 Chapter 3: Investment governance

The investment of fund assets is one of the key parts of the role played by a trustee of a superannuation fund. The governance of the investment function is key in ensuring that the steps involved in the investment process are efficient and that risk is managed properly at all levels.

The Panel recognises that the investment of a modern superannuation fund is a complex activity requiring a wide range of technical expertise and skills. For this reason, most APRA-regulated funds employ a range of service providers, including fund managers, asset consultants and custodians, to assist them. This in turn places pressure on the trustee to ensure that the process of appointment and the process of monitoring these ‘agents’ are designed to promote the interests of members.

The Panel has identified a number of areas in which a measure of tightening in the regulatory system seems appropriate.

Performance-based fees were, until recently, typically only charged by hedge funds or in the context of mandates relating to alternative assets. Quite quickly, they have become much more widespread. The Panel’s view is that performance-based fees should be the exception, rather than the rule, for superannuation fund investments and has recommended that a performance-based fee standard be adopted for MySuper products.

Members accumulate their retirement savings and retire on after-tax returns, not pre-tax ones. Yet, there is a wide variation in the extent to which most trustees and investment managers have regard to the optimisation of tax outcomes for members. The benefits of dividend imputation credits and capital gains tax discounts are only realised where the underlying investments are held at the time of the dividend distribution, or for a specified period.

Investment ‘churn’ or portfolio trading that ignores tax consequences can result in the premature turnover of assets where the potential after-tax benefits to members are lost.

Research on the quantum of the leakage has found that portfolio turnover resulting from investment decisions made without regard to tax can affect after-tax returns significantly. The Panel believes that the SIS Act should be amended so that trustees have an obligation to have regard to the tax consequences of their investment strategies.

Similarly, the Panel also considers that the SIS Act should be amended so that trustees have an obligation to have regard to the expected costs of particular investment strategies and the availability of independent and timely asset valuations.

5.4 Chapter 4: Outcomes transparency

Transparency and comparability are critical to the efficiency and operation of a market-based savings system, even where participation is compulsory. The Panel believes that there is presently a lack of transparency, comparability and, ultimately, accountability in the Australian superannuation system that can only be effectively improved through targeted and proportionate regulation.

The Panel considers that, to make progress quickly toward accurate comparability, APRA should have a new power to make 'outcomes reporting standards' as to the way large APRA funds report and advertise the investment performance and costs of their investment options. Large APRA funds would be required (among other things) to:

- report past performance in a standard format that also discloses the volatility associated with the return; and
- classify their investment options according to a new 'risk and return targeting' approach.

In financial markets, there is great benefit in what could be termed 'systemic transparency': that is, disclosure to the system at large, including regulators, academics, analysts, advisers and informed investors. 'Systemic transparency' is what is largely missing in the Australian super system. There is too little high quality information available to experts who would be able to use such information for the ultimate benefit of members as a whole. Systemic fund information about large APRA funds should sit alongside specific member-focused and event-driven disclosure obligations.

The Panel considers that there needs to be a low-cost, but dramatic, change in this area. This is where large APRA funds must see themselves as different from other businesses. Trustees must get used to being more transparent about their funds. The Panel therefore believes there should be new standards for web-based systemic disclosures for large APRA funds in a range of areas, including details of their portfolio holdings every six months.

Members also need a certain minimum amount of information when considering superannuation investment options, including MySuper. The Panel believes this can be provided through the development of a plain English product 'dashboard' that would provide members with a standardised format in which to compare:

- the investment option's risk and return targets;
- whether the investment option was illiquid; and
- fees and costs, including a projected Total Annual Expense Ratio (**TAER**).

5.5 Chapter 5: Insurance in superannuation

Insurance can be an important aspect of superannuation as it provides benefits to members (and their dependants) when members are no longer able to work due to death or total and permanent disablement (**TPD**) before normal retirement age.

However, insurance cover embedded in super comes at the cost of foregone retirement savings and earnings. In this context, trustees have an important role in setting appropriate insurance offerings for their members. Default insurance must be tailored for members who do not consider their insurance needs, and who rely on the trustee's judgment for adequate insurance. For members who do consider their insurance needs, they should be able to opt-out of cover entirely or to have access to additional cover.

Death and TPD insurance, in particular, meet the needs of members so that they have sufficient benefits in the event that they need to access their retirement savings early. Income protection insurance can complement these types of insurance by providing benefits when disability is believed to be temporary, not permanent. In the Panel's view, no other type of insurance is consistent with the objectives of superannuation and nor should it be paid for from member super savings.

Insurance is a complex product for member and trustee alike and it is a crucial component of superannuation. Accordingly, all trustees should develop a considered insurance strategy and monitor its implementation. The risks associated with fund self-insurance of life and TPD benefits are high and so self-insurance should only be permitted in limited circumstances.

Information about insurance must be more widely available and trustees must make it easier for members to compare insurance options, recognising the financial impact on members. The Panel thinks that much of this can be easily accomplished on the fund's website.

In superannuation, insurance is generally automatically provided to members and, consequently, members will continue to have coverage without the need to have advisers renumerated by trailing commissions. In the Panel's view, commissions add unnecessarily to the insurance premiums that members pay.

5.6 Chapter 6: System integrity

Trustees of large APRA funds need direct access to a risk-weighted pool of capital, whether an operational risk reserve within the fund or capital held separately by the trustee. Changes proposed in order to improve access to capital according to the assessed risk of the fund should be phased in over time so as to lift prudential standards while minimising any inter-generational equity issues and disruption to funds.

Trustees need to give explicit consideration to liquidity risk management at both whole of fund and investment option level.

Administrators and commercial clearing houses are systemically significant to the superannuation system and should be subject to APRA regulation and licensing, including a requirement to hold capital in their own right.

The funding standards for defined benefit funds should be strengthened to focus on the level of vested benefits rather than minimum requisite benefits. The Panel believes that defined benefit funds need to be considered carefully and specifically when there is any change to legislation as costs for these funds can be inadvertently increased when legislation does not sufficiently take them into account.

Given the superannuation system's sole purpose, externalities, whether a national interest in developing infrastructure, or promoting sound environmental, social and governance outcomes, always need to be reflected in the risk and return valuation of a potential investment, but not as ends in themselves.

5.7 Chapter 7: Retirement

Australia's superannuation system exists to deliver private income to enhance the living standards of retired Australians. Successive governments have committed to the 'three pillar' framework as the underpinning of Australia's retirement incomes policy, blending near-universal employee participation in the superannuation system with an adequate social security safety net and incentives for discretionary savings by individuals beyond the employer-mandated levels.

To date, the retirement income product market has been under-developed, largely reflecting the relatively small balances that many retiring workers hold as a consequence of the immaturity of the SG system (being less than 20-years old). Currently, the market is dominated by account-based products in which the risks associated with investment markets, longevity and inflation are directly borne by the member. However, balances will increase substantially in the period ahead and this, combined with demographic ageing, should help spur product development. Treasury estimates that post-retirement assets will more than triple in real terms by 2035 to reach $850B.

MySuper should be a whole of life product and include a single type of retirement income stream product, chosen by the trustee.

Because retirement needs vary considerably, there is no 'one-size-fits-all' retirement income product that the government should mandate. It is important that trustees consider longevity issues more explicitly when developing investment strategies. It is also important that the regulatory system supports product innovation.

Good financial advice can be very helpful as members plan for retirement and as they manage assets in the retirement phase. There is a strong case for requiring MySuper products to provide proactive intra-fund advice periodically to this group of members.

5.8 Chapter 8: Self-managed super solutions

The Panel recognises that within the SMSF sector, members (who also act as the trustees) should have ultimate responsibility for their retirement savings. Unless there is a countervailing public policy reason, trustees of SMSFs should be free, as much as possible, from government intervention.

In effect, the work of the Panel has led it to conclude that the SMSF sector is largely a successful and well-functioning part of the system, as reflected in the Panel's statistical summary issued in December 2009. In fact, the Panel suspects that the most significant aspect of its work in the SMSF sector is what it has not recommended (for example, minimum fund size or specific trustee educational requirements). The SMSF recommendations are not dramatic and largely relate to compliance, audit, adviser competency and like measures. There were some recommendations about assets that the Panel thought ought not to be in SMSFs (for example, collectables) but these were not material in quantum.

Some trustees are capable of looking after all of the affairs of their SMSF. Most ultimately delegate some or all of the tasks of running an SMSF to service providers. In some respects, service providers in the SMSF sector have a unique role. They are, in a sense, the first line of defence for the community in a sector that is characterised by a do-it-yourself philosophy. Recognising this, the Panel believes that higher competency and advice standards are needed for SMSF service providers. The Panel also believes that the sector would be more efficient if trustees had access to better resources and simplified legislation.

The Panel also recognises that other parts of the SMSF regulatory framework need to be improved. The ATO needs a greater range of flexible penalties if it is to achieve appropriate and proportionate regulatory outcomes. Likewise, given the pivotal role approved auditors play in underpinning the SMSF regulatory framework, their competence and independence should be raised to a level where they provide the level of assurance that a compliance-based regulatory framework demands. The SMSF registration process needs to be improved to combat frauds and illegal early access schemes.

5.9 Chapter 9: SuperStream

'SuperStream' is the name the Panel has chosen to describe the package of measures designed to enhance the current 'back office' of superannuation. It includes new standards to improve the quality of data provided by employers, to allow the use of tax file numbers (**TFNs**) as a primary identifier and to require the use of technology to improve processing efficiency. SuperStream also includes improvements to the way fund-to-fund rollovers are processed and the way contributions are made.

Excessive costs caused by manual processing of both money transfers and data in super can be significantly reduced by requiring electronic transmission of linked financial and member data at all levels, using standardised formats. Use of the TFN as the primary identifier is critical to this process.

There will be an enhanced role for the ATO in facilitating a more efficient back office for superannuation. Further, the Panel proposes that the present array of controls over superannuation contributions should be simplified and streamlined, with the ATO having sole regulatory responsibility.

Improved data quality and search processes should lead to a reduction in the number of inactive or lost member accounts in the system.

5.10 Chapter 10: Regulatory settings

Changes are required to the regulatory system in order to achieve the efficiencies that the Panel seeks for the industry.

The Panel believes that APRA must have a standards-making power in relation to superannuation to allow it to take on the significant tasks of overseeing and promoting industry efficiency (as well as its existing prudential role). The Panel sees this complemented by a fresh approach to graduated regulatory enforcement and sanctions.

The Panel is of the view that efficiency can also be achieved by enhanced cooperation and coordination between the regulators with respect to their superannuation functions. This could take several forms, including secondment arrangements between ASIC and APRA or an operational merger of their superannuation capabilities with or without a co-location in major offices. The ATO should be resourced so that it can carry out its new role with respect to SuperStream as well as its current roles in the industry.

In the Panel's view, further efficiencies can be achieved by facilitating rationalisation of legacy products in superannuation and, to that end, suggests that the equivalence test for successor fund transfers be changed to a test of 'no overall disadvantage' with the intention of allowing more transfers to proceed. There is also benefit in giving the Federal Court the jurisdiction to determine superannuation product rationalisation where the successor fund transfer test cannot be met. CGT relief in these instances should be expanded and made permanent.

Inefficiency is also a by-product of a complex legislative framework and the Panel believes that a restructure of the SIS Act could be helpful to the industry. The Panel suggest that the SIS Act be organised so that, among other things, the provisions applying to each sector of the new choice architecture are set out separately.

As a way to determine if the Panel's recommendations have been effective in advancing efficiency in the industry, the Panel believes that the Productivity Commission should review the impact and implementation of MySuper and SuperStream and the functioning of the retirement product market five years after the Government's response to this report.

With a view to advancing members' interests, the Panel believes that 'member protection' should cease in the new choice architecture so that subsidisation of 'protected' members by 'unprotected' members does not continue to occur. The Panel also endorses an extension of the General Employee Entitlement and Redundancy Scheme (**GEERS**) to cover up to three months of unpaid SG Act contributions and a change of name for the Superannuation Complaints Tribunal (**SCT**) to become the 'Superannuation Appeals Tribunal' to better reflect its role.

6 HOW THE RECOMMENDATIONS BENEFIT MEMBERS

The Panel's terms of reference were quite explicit that its work was to be '*conducted around the concepts of the best interests of the member and the maximising of retirement incomes for Australians*'.

The Panel has therefore framed its recommendations in a way that reinforces the principle that superannuation must be for the benefit of members and imposes new requirements on trustees to ensure that they make decisions and conduct their operations so that members benefit.

The Panel has also developed numerous proposals to make super easier, simpler and more efficient for members.

6.1 Optimising costs and fees for members

6.1.1 MySuper fees in current market conditions

The aim of MySuper is lowering overall costs for members while supporting and encouraging a competitive market-based, private sector infrastructure for superannuation. The Panel's objective is to make super better value for money and MySuper is designed with this in mind.

While the Panel has not recommended a cap on fees, the Panel has recommended changes in legislation and regulation to make fees more transparent and to assist members to compare fees across the industry. These measures, along with sharper duties on trustees, should see better management of overall costs.

As part of the Review, the Panel commissioned a report from Deloitte Actuaries and Consultants seeking Deloitte's view of reasonable and achievable total costs for an average member with a $25,000 account balance, assuming the adoption of the MySuper model. Deloitte's methodology involved using current market information to estimate the likely costs and fee ranges for the various components of the MySuper product, without taking account of the impact of SuperStream and other Panel recommendations.

Deloitte's view of what the current market could provide in the way of fees for MySuper is shown in the following table:

Table 2: Estimated total annual percentage costs for MySuper products of varying sizes (investment costs, plus operating costs and intra-fund advice)

MySuper fund size/investment strategy	$2b	$5b	$10b	$20b
Passive balanced	0.60%	0.46%	0.38%	0.32%
Passive conservative	0.58%	0.45%	0.37%	0.32%
Active balanced	0.94%	0.83%	0.70%	0.60%
Active conservative	0.80%	0.70%	0.59%	0.49%
Active balanced (with alternatives)	1.04%	0.89%	0.77%	0.66%
Active conservative (with alternatives)	0.89%	0.76%	0.64%	0.54%

A copy of the full Deloitte report is at appendix D.

For a variety of reasons, fees currently paid by super fund members cover a wide range across the different fund types and sectors. However, nearly all default fund members are today paying more than the 0.66 per cent total fees projected by Deloitte for the highest cost investment option in a $20B MySuper product, with some members paying more than twice this amount. This estimated saving would represent a significant boost to retirement savings. Treasury estimates an average fee for default fund members of 97bps per annum, based on the Rice Warner *Superannuation Fee Report 2008*.

Being a current market estimate, Deloitte's numbers do not take account of any savings from the SuperStream proposal to modernise the 'back office' of the super industry (see chapter 9). The Panel asked Deloitte to keep the account balance used in the examples low, reflecting the relatively low average account balances in the system. An account balance of $250,000 would see operating costs, including for intra-fund advice, of between 0.05 per cent for a $2B fund and 0.03 per cent for a $20B fund, to which percentage-based investment management fees would have to be added.

6.1.2 Would lower fees harm investment returns?

Concern has been expressed that MySuper would be seen as 'cheap and nasty' with its members disadvantaged because they would be forced into poorly-performing low cost investment strategies. This is not so. The cost estimates shown in table 2 include an element of performance fees and range across passive and active investment strategies, including exposure to alternative asset classes.

MySuper trustees would be required to consider and implement, as appropriate, what they consider to be the optimal investment strategy to maximise net returns for their members.

There is no justification for the assertion that MySuper would prevent trustees and fund managers from pursuing certain types of investment strategies that they might otherwise consider. The MySuper concept is predicated on trustees being required to design and implement an investment strategy that is for the benefit of members, which means trustees have to weigh the expected returns of any strategy against considerations of liquidity, risk and cost. The Panel is confident that trustees would be able to identify strategies that offer competitive net (that is, after taxes, fees and costs) returns to members within the regulatory framework governing MySuper.

It is clear from Deloitte's work, and other material analysed by the Review, that there are substantial benefits from scale in the super industry. In MySuper, trustees would have to consider annually whether their MySuper product would have enough scale to provide optimal benefits to members.

6.1.3 Future impact of MySuper and SuperStream on fees

The Panel has sought to quantify (as set out in table 3) the potential impact of two major reforms – MySuper and SuperStream on fees that members might pay in the future.

Table 3: Projected annual savings from MySuper and SuperStream*

Source of savings	Short-run	Long-run
MySuper	$0.55b	$1.7b
SuperStream	$1.0b	$1.0b
Total annual savings	**$1.55b**	**$2.70b**

* The SuperStream reforms are expected to involve initial up-front costs for the industry and the full benefits might not be realised immediately. These short-run costs have not been quantified. However, they are expected to be relatively low in the longer term.

These fee savings would provide significant benefits to ordinary workers. Treasury estimates that an average wage earner paying average MySuper fees could benefit from around a 40 per cent fee cut, lifting their final superannuation balance by around $40,000 or 7 per cent.

Given the uncertainties involved, these estimates should be seen as broadly indicative only. Details of the Treasury assumptions underpinning these projections are set out in appendix C.

6.2 Better retirement benefits

The better management of costs and fees goes directly to improving the bottom line for members, that is, greater retirement benefits. The information in section 6.1 illustrate what positive results can be achieved with the MySuper and SuperStream proposals.

While increased retirement benefits are the overall aim of the Panel's recommendations, specific recommendations that significantly contribute to this result are:

(a) movement of a greater share of the value derived from investments of super assets from agents to members as competition, scale and efficiency gains are realised, increasing members' net wealth;

(b) prohibiting adviser commissions on insurance provided through superannuation, that can be up to 20-30 per cent of member premiums;[16]

(c) removing trailing commissions on advice and limiting performance-based investment management fees;

(d) requiring trustees to manage investments for after-tax returns and to align investment management arrangements with member interests;

(e) giving MySuper trustees a duty to consider longevity risk and inflation risk in relation members in retirement phase;

(f) removing barriers in the tax legislation and SIS Act to fund consolidation so that scale can be more easily achieved; and

(g) requiring trustees to have not only an investment strategy, but also an insurance strategy so that costs in both areas are actively considered and managed by the trustee.

6.3 Enhanced security of the system

Imposing a capital (or reserving) requirement on trustees will help ensure their viability, which is of course of utmost importance to members.

Licensing of administrators and clearing houses (and capital requirements for them) means that member records are more secure and, generally, reduces the risk of operational failure in administrators and clearinghouses. Bringing these entities into the regulatory net gives comfort to members that the regulatory oversight extends to all critical operations of the system.

Defined benefit members will be more secure in knowing that the focus of funding will be on their vested benefits not minimum requisite benefits.

Further, trustees will be required to manage liquidity risks better both in the fund as a whole and in individual investment options which reduces the risk for members that there will be no cash available to pay their benefits when they come due.

The strengthening of governance standards for trustee boards and trustee-directors will help ensure that persons involved with the fund at the highest level are of high quality and capability.

Maintaining confidence in the system is important and securing the system's stability is fundamental.

6.4 Better information

Increasing the transparency of the system and providing more meaningful information would be of obvious benefit to members. The Panel believes that the provision of better information to members and their advisers would make superannuation less opaque and increase the likelihood that members understand what is happening with their superannuation.

The new 'forward looking' investment option disclosure 'dashboard' would enable members to examine likely future performance, rather than basing investment choice on past investment performance. The Panel believes that this way of preparing and disclosing investment option data will aid members in figuring out some of the technical information that is associated with their super.

MySuper trustees will be required to provide their members with intra-fund advice proactively at various stages throughout their working lives and as they approach retirement and during their retirement. The Panel sees intra-fund advice as being of great value to members as it comes from the trustee, the entity that is most familiar with the fund's operation.

6.5 Greater efficiency

As a consequence of the SuperStream proposals, super will be easier to locate and harder to lose.

Currently, there are approximately 12M members with superannuation,[17] yet there are over 33 million accounts.[18] Equally frustrating for members (and trustees and administrators) is the laborious process of reuniting members with their 'lost' super. There was more than $13.6B in lost super as at 30 June 2009.[19]

The Panel's recommendations to enable greater use of TFNs to help in identifying member accounts, to require electronic transmission of linked financial and member data (using standardised formats) and to facilitate auto-consolidation of multiple accounts will go far in making the system more efficient for members.

Members will also benefit from the Panel's emphasis on the availability of electronic information both from their fund and from government. The establishment of the government's super website means that there will be a central, authoritative repository for information about superannuation. A website-based approach will be more efficient (and less costly) as information can be updated easily and quickly and members can access the information at any time.

7 IMPLEMENTATION

While pitching its recommendations at a high conceptual level, the Panel has endeavoured throughout the Review to be satisfied that its ideas and recommendations are practicable. In part, this has been in an effort to minimise any unintended consequences of its proposals.

The Panel appreciates the work involved in taking high level recommendations and implementing them in practice. To that extent the Panel has, where possible, given as much direction as it can to enable the Treasury, with its responsibility for implementing recommendations that are accepted by Government, to understand the Panel's thinking. In the same vein, the Panel urges Treasury to have regard to the 10 super policy principles to clarify areas of ambiguity.

Inevitably, there will be matters of detail that will not be addressed in a project of this nature and these will have to be resolved in the subsequent consultation process.

The Panel's recommendations are expected to benefit members substantially in the long term through cost savings and improved efficiencies. Counter-balancing these savings, the Panel acknowledges that some of its recommendations would increase some fund costs in the short term, particularly the implementation of certain aspects of the MySuper and SuperStream reforms.

When making recommendations, the Panel has been conscious of the Government's best practice regulation principles. As a result, the Panel's largely principle-based reforms aim to maximise the overall benefit to members, while minimising the cost borne by the industry.

The Panel has not presumed to recommend a specific timetable or sequence of implementation, although it would clearly be preferable for implementation planning to commence immediately on some of the key proposals including MySuper and the various SuperStream proposals. Many of the other key recommendations depend on further detailed consultation with the industry, and any reforms requiring legislative changes need to be very carefully planned and accommodated within the government's broader legislative program. The Panel is, however, confident that all the reforms proposed are eminently capable of being implemented, and will result in significant net gains to members.

8 OUTSTANDING ISSUES

As part of the Review process, the Panel released three comprehensive issues papers, detailing myriad issues about governance, operations, efficiency and structure across the superannuation industry today (see appendix A for a list of the issues papers).

The Panel's priority has been to address those issues that it believed would bring about the greatest benefit to members and the superannuation industry. However, the Panel recognises that there are still a number of second order, but still important, changes that could result in benefits for members. In this regard, the Panel believes that policy makers and regulators should continue to progress these issues and commends to them the issues papers – and the submissions that responded to these papers — as an important on-going resource.

9 ACKNOWLEDGEMENTS

The Panel wishes to thank the large number of organisations, particularly APRA, the ATO, ASIC and everyone who participated in roundtables, focus groups and meetings with the Panel, or assisted with research. The Panel was grateful to receive the many thoughtful, considered and useful submissions and thanks the many organisations who made submissions in all three phases of the Review. The Panel was also particularly grateful that so many individual members made submissions about their own experiences and issues.

The Panel also acknowledges the support Minister Bowen and the Government have given to the Review process, while always respecting the independence of the Panel. The Panel also acknowledges the initiative of Assistant Treasurer, Senator the Hon Nick Sherry, in instigating the Review.

The Panel is also grateful for the administrative support it has received from many areas of the Department of the Treasury. There were also many other supporters of the Review who assisted in various ways during the process (by providing meeting venues, ideas and feedback, good quality coffee, discussion forums and support) and we thank them as well.

There were many friends of the Review (too many to name individually) and the Panel thanks each of them for their support and encouragement.

Lastly, the Panel wishes to acknowledge the outstanding support provided by all members of the Review secretariat (listed in appendix E) drawn from both the private and public sectors.

10 LIST OF RECOMMENDATIONS

10.1 Chapter 1: MySuper and choice architecture

Recommendation 1.1

The 'choice architecture model' should be adopted as the structure for Australia's superannuation industry.

Recommendation 1.2

The SG Act should be amended so only a MySuper product is eligible to be a 'default' fund nominated by an employer.

Recommendation 1.3

The relevant legislation should be amended so:

(a) only MySuper products are eligible to be nominated; and

(b) all MySuper products are able to be nominated,

for 'default fund' purposes in awards approved by Fair Work Australia.

Recommendation 1.4

In 2012, the Productivity Commission should conduct a review of the processes by which default funds are nominated in awards to assess whether the processes are sufficiently open and competitive.

Recommendation 1.5

Any fund that is a 'successor fund' (as defined in the SIS Act) to a fund currently nominated as a default fund under an award should, where the successor fund is a MySuper product, be accepted automatically as a default fund under the award, so that there is no impediment to consolidation for those funds that wish to do so.

Recommendation 1.6

The SIS Act should be amended to apply statutory duties to MySuper trustees to:

(a) formulate and give effect to a single, diversified investment strategy at an overall cost aimed at optimising fund members' financial best interests, as reflected in the net investment return over the longer term; and

(b) actively examine and conclude whether, on an annual basis, its MySuper product has sufficient scale on its own (with respect to both assets and number of members) to continue providing optimal benefits to members.

Recommendation 1.7

The SIS Act should be amended to require trustees of MySuper products to satisfy objective criteria relating to:

(a) APRA licensing;

(b) acceptance of contributions;

(c) single, diversified investment strategy;

(d) absence of costs cross-subsidisation;

(e) buy and sell spreads;

(f) switching fees;

(g) fee discounts;

(h) performance-based investment management fees;

(i) e-super disclosures;

(j) retirement income stream product;

(k) entry and exit fees;

(l) benchmarking;

(m) intra-fund advice;

(n) insurance;

(o) absence of commissions and like payments; and

(p) member engagement.

Recommendation 1.8

Neither advice to members (other than intra-fund advice), nor advice to employers should be 'bundled' with MySuper products.

Recommendation 1.9

Advice to members of a MySuper product (other than intra-fund advice) should only be provided on request and trustees should only be able to deduct the costs of advice about superannuation from a member's account with the member's written agreement.

Recommendation 1.10

The cost of advice or services provided to employers should not be borne in any way, directly or indirectly, by MySuper members.

Recommendation 1.11

Trustees of MySuper products should not:

(a) pay or fund any product-based up-front or trailing commission or other similar payment; or

(b) make or fund any payment that relates to volume,

in respect of superannuation advice or other products or services provided to members.

Recommendation 1.12

Members of MySuper products should only be provided with advice about superannuation (other than intra-fund advice) under arrangements that require the member to renew the advice service each year on a renewal notice from the adviser.

Recommendation 1.13

ASIC should, in consultation with industry, devise a standard form which requires clear identification of the advice service to be provided where a fund member renews an ongoing advice service.

Recommendation 1.14

Trustees of MySuper products should not pay premiums for insured member benefits that include or fund an up-front or trailing commission or like payment.

Recommendation 1.15

Legislation should apply specific and thorough conduct and enquiry duties on persons (including trustees) providing switching advice to a MySuper member built on the current requirements of section 947D of the Corporations Act.

Recommendation 1.16.

Members should only be able to be moved involuntarily out of a MySuper product if they are:

(a) transferred to an ERF;

(b) flipped from a MySuper product in a master trust to another MySuper product in another division of that trust; or

(c) transferred under legislative requirements such as auto-consolidation of accounts or temporary resident arrangements.

Recommendation 1.17

The presentation of retirement forecasts should be mandatory for MySuper products, and should be developed in consultation with industry in accordance with the approach identified by the Panel.

Recommendation 1.18

The superannuation industry should have at least two years to transition to MySuper and the new choice architecture.

Recommendation 1.19

Both APRA and ASIC should oversee the transition referred to in Recommendation 1.18.

Recommendation 1.20

Trustees of choice sector products should also not be able to charge entry fees and should only charge exit fees on a cost recovery basis.

Recommendation 1.21

Neither advice to members (other than intra-fund advice), nor advice to employers should be bundled with choice products or with any other product in the choice architecture model, including products offered to SMSFs.

Recommendation 1.22

Advice to members of a choice product or of any other product in the choice architecture model (other than intra-fund advice) should only be provided on request and trustees should only be able to deduct the costs of advice about superannuation from a member's account with the members' written agreement.

Recommendation 1.23

The costs of advice to employers should not be borne in any way, directly or indirectly, by members of choice products or by members of any other products in the choice architecture model.

Recommendation 1.24

Trustees of choice products or of any other product in the choice architecture model should not:

(a) pay or fund any product-based up-front or trailing commission or other similar payment; or

(b) make or fund any payment that relates to volume,

in respect of superannuation advice or other products or services provided to members.

Recommendation 1.25

Members of choice products or of any other product in the choice architecture model should only be provided with advice about superannuation (other than intra-fund advice) under arrangements that require the member to renew the advice service each year on a renewal notice from the adviser.

Recommendation 1.26

Trustees of choice products or of any other product in the choice architecture model should not pay premiums for insured member benefits that include or fund an up-front or trailing commission or like payment.

Recommendation 1.27

Choice trustees must offer a range of options sufficient to allow members to obtain a diversified asset mix if they choose, but members can choose to be undiversified and the trustee would have no obligation to assess the appropriateness of the investment strategy chosen by the member. Trustees would be subject to new express duties in selecting and monitoring options.

Recommendation 1.28

A choice trustee that discharges its duties in selecting and monitoring investment options should not be exposed to civil liability in the event that a member suffers damage by reason of illiquidity or other circumstances affecting the investment option, including diminution in value or failure.

10.2 Chapter 2: Trustee Governance

Recommendation 2.1

The SIS Act should be amended to create a distinct new office of 'trustee-director' with all statutory duties (including those which would otherwise be in the Corporations Act) to be fully set out in the SIS Act, along with re-focused duties for trustees. The duties for trustee-directors should include:

(a) To act solely for the benefit of members, including and in particular:

- **i. to avoid putting themselves in a position where their interests conflict with members' interests;**
- **ii. to give priority to the duty to members when that duty conflicts with the trustee-director's duty to the trustee company, its shareholders or any other person;**
- **iii. to avoid putting themselves in a position where their duty to any other person (such as another super fund or a service provider) conflicts with their duty to members;**
- **iv. to avoid putting themselves in a position where their duty to any other person (other than members) conflicts with their duty to the trustee company;**
- **v. not to obtain any unauthorised benefit from the position of trustee or trustee-director; and**
- **vi. not to enter into any contract, or do anything else, that would prevent the trustee from, or hinder the trustee in, properly performing or exercising the trustee's functions and powers.**

(b) To act honestly.

(c) To exercise independent judgment.

(d) To exercise the degree of care, skill and diligence as an ordinary prudent person of business would exercise in dealing with the property of another for whom the person felt morally bound to provide.

(e) To have specific regard to (among other matters) the likely long term consequences of any decision, including the impact of the decision on the community and the environment and on the entity's reputation for high standards of conduct.

The duties for trustees should include:

(f) To keep the money and other assets of the entity separate from any money and assets, respectively:

i. that are held by the trustee personally; or

ii. that are money or assets, as the case may be, of a standard employer-sponsor or an associate of a standard employer-sponsor, of the entity.

(g) To formulate and give effect to an investment strategy in respect of the fund as a whole and each investment choice option, that has regard to the whole of the circumstances of the entity including, but not limited to, the following:

i. the risk involved in making, holding and realising, and the likely return from, the entity's investments having regard to its objectives and its expected cash flow requirements;

ii. the composition of the entity's investments as a whole, including the extent to which the investments are diverse or involve the entity in being exposed to risks from inadequate diversification;

iii. the liquidity of the entity's investments having regard to its expected cash flow requirements;

iv. the ability of the entity to discharge its existing and prospective liabilities;

v. the expected costs of the strategy, including those at different levels of any interposed legal structures and under a variety of market conditions; and

vi. the taxation consequences of the strategy, in light of the circumstances of the fund.

(h) To formulate and give effect to an insurance strategy which includes, but is not limited to, the types of insurance to be offered and the default minimum and permissible maximum levels of cover to be offered as well as the cost and value for money to members.

(i) If there are any reserves of the entity, to formulate and to give effect to a strategy for their prudential management, consistent with the entity's investment strategy and its capacity to discharge its liabilities (whether actual or contingent) as and when they fall due.

(j) To allow a beneficiary access to any prescribed information or any prescribed documents.

(k) To act fairly between all beneficiaries of the fund and to act impartially between beneficiaries of the same class.

Recommendation 2.2

Trustee-directors should not be required to have specific pre-appointment skills or training. However, APRA should consider further strengthening it's administration of the 'fitness' test under the SIS Act including requiring potential trustee-directors to be fully briefed before accepting the position (or deciding to seek nomination, where applicable) as to their responsibilities and potential liabilities. The Code of Trustee Governance should address the on-going training requirements that trustees and trustee-directors must meet on an annual basis.

Recommendation 2.3

The board of the trustee must demonstrate on an annual basis that it has the collective skill set to govern the APRA-regulated fund or funds for which it is responsible and this should be one of the subjects covered in the independent annual review of the board.

Recommendation 2.4

The SIS Act should be amended so that it is no longer mandatory for trustee boards to maintain equal representation in selecting its trustee-directors. The Panel expects that trustees would review and amend corporate constitutions to ensure consistency with this recommendation.

Recommendation 2.5

The SIS Act should be amended so that policy committees are no longer mandatory where the trustee board does not have equal representation.

Recommendation 2.6

The SIS Act should be amended so that if a trustee board does not have equal representation, the trustee must have a majority of 'non-associated' trustee-directors (as described in chapter 2).

Recommendation 2.7

For those boards that have equal representation because their company constitutions or other binding arrangements so require, the SIS Act should be amended so that no less than one-third of the total number of member representative trustee-directors must be non-associated and no less than one-third of employer representative trustee-directors must be non-associated.

Recommendation 2.8

The Corporations Act should be amended so that any provision of a trustee company constitution that prohibits any trustee-director from voting on any trustee company business (other than in the event of conflict of duty or interest) is ineffective.

Recommendation 2.9

SIS Act section 101 should be amended to require a trustee to provide a member with reasons for its decision in relation to the member's formal complaint.

Recommendation 2.10

Section 197 of the Corporations Act should have no application to a director of a company to the extent that the company is acting as a trustee of an RSE and the Corporations Act should be amended accordingly.

Recommendation 2.11

All trustees should be required, as a condition of their RSE licence, to have an appropriate level of indemnity insurance cover and to provide an annual certificate of currency to APRA.

Recommendation 2.12

The enforcement provisions of the SIS Act and the Corporations Act should be reviewed and an appropriate proportionate penalty regime should be designed to take into account the new duties imposed on trustees and trustee-directors.

Recommendation 2.13

In order for a trustee-director to act as a trustee-director on the board of more than one APRA-regulated fund, the person and both boards need to attest to APRA that at the time of appointment there is no reasonably foreseeable conflict between the person's duty to the members of each fund and to the person's duty to each trustee company. There would be a transitional period for existing trustee-directors with multiple board positions. APRA would need the appropriate regulatory tools to administer this requirement.

Recommendation 2.14

The SIS Act should be amended so as to override any provision in the governing rules of an APRA-regulated fund that requires the trustee to use a specified service provider in relation to any services in respect of the fund.

Recommendation 2.15

A record of all gifts, emoluments and benefits (subject to an appropriate materiality threshold) provided to trustees, trustee-directors and management should be kept in a register maintained by the trustee and disclosed to APRA annually as well as in the annual fund report to members and on the fund's website.

Recommendation 2.16

APRA should develop a prudential standard that sets out particular examples of conflicts of interest and conflicts of duty to illustrate behaviour that would not be allowed in relation to all APRA-regulated funds so as to ensure that trustee-directors and trustees observe their duty of loyalty to members.

Recommendation 2.17

Trustees of APRA-regulated funds should, as a condition of their RSE licence, be required to articulate and follow a conflicts policy specifically tailored to their business structure that addresses all relevant issues regarding their role under the SIS Act and as a fiduciary to the members of the fund.

Recommendation 2.18

An industry council (coordinated by APRA) should develop, in consultation with all stakeholders, a Code of Trustee Governance for trustees of superannuation funds and their trustee-directors to assist with identifying best practice in the industry. The Code could cover, but not be restricted to:

(a) the imposition of a higher standard of competence and a greater commitment of time from those appointed to chair a super fund board than is required of other trustee-directors;

(b) board size, including whether a maximum is appropriate and any transition period for successor fund transfers and mergers;

(c) length of time in office and retirement by rotation;

(d) development of an enhanced conflicts-handling policy, including maintenance of an affected-decisions register and regular reporting to APRA;

(e) skill set for each director to demonstrate within the first 12 months of appointment;

(f) a skill matrix for the trustee board and analysis of how the current composition of the board provides the skills required under the matrix;

(g) a procedure for a rigorous and independent annual review of the performance of each trustee-director and the overall collective competence and performance of the board;

(h) gender and other diversity requirements;

(i) tendering for and benchmarking service providers; and

(j) minimum ongoing training requirements.

Recommendation 2.19

If industry cannot work together to establish such an industry council, or cannot finalise a Code of Trustee Governance within two years, then APRA should create the Code.

Recommendation 2.20

There should be an annual audit of the trustee's performance against the requirements of the Code of Trustee Governance and the results of that audit should be made available on the fund's website.

10.3 Chapter 3: Investment Governance

Recommendation 3.1

That section 52(2)(f) of the SIS Act be amended to include 'the expected costs of the strategy, including those at different levels of any interposed legal structures and under a variety of market conditions', as one of the factors to which APRA fund trustees must 'have regard'.

Recommendation 3.2

An enforceable 'performance fee standard' should be developed by APRA in consultation with industry.

Recommendation 3.3

No performance-based fees may be paid by the trustee of a MySuper product unless the payment conforms with the 'performance fee standard'.

Recommendation 3.4

That section 52(2)(f) of the SIS Act be amended to include 'the taxation consequences of the strategy, in light of the circumstances of the fund', as one of the factors to which APRA fund trustees must 'have regard', and to ensure that trustees consider those taxation consequences when giving instructions in mandates to investment managers.

Recommendation 3.5

That section 52(2)(f) of the SIS Act be amended to include 'the availability of valuation information that is both timely and independent of the fund manager, product provider or security issuer', as one of the factors to which APRA fund trustees must 'have regard'.

Recommendation 3.6

All large APRA funds should publish their proxy voting policies and procedures, and disclose their voting behaviour to members on their websites.

10.4 Chapter 4: Outcomes transparency

Recommendation 4.1

With an enhanced rule-making power, APRA, in consultation with ASIC and industry, should develop outcomes reporting standards as an overlay to the existing accounting standards AAS 25 and ED 179 to facilitate consistent and comparable reporting by large APRA funds of investment performance and costs at investment option level, including for MySuper products.

Recommendation 4.2

In addition to whole of fund reporting, APRA should publish investment return performance data for MySuper products.

Recommendation 4.3

All funds should be required to publish on their websites an investment option performance table (as shown in table 4.1 in chapter 4) showing investment returns and costs at investment option level, in accordance with an outcomes reporting standard to be developed by APRA in consultation with ASIC and the industry.

Recommendation 4.4

APRA should be the sole public sector agency responsible for collecting data for all public purposes in respect of all APRA funds and EPSSSs. APRA should have the primary responsibility for the publication of all superannuation data in as disaggregated a form as is consistent with privacy principles.

Recommendation 4.5

The ATO should continue to collect data in relation to SMSFs.

Recommendation 4.6

It should be mandatory, when referring to past performance of a MySuper product or a choice investment option, to disclose a standardised measure of the uncertainty or volatility associated with the return (an example of which is shown in table 4.1 in chapter 4). This requirement, and the volatility measure to be used, should be in an outcomes reporting standard to be developed by APRA in consultation with ASIC and the industry.

Recommendation 4.7

All forms of cost and fee disclosure by superannuation funds should be on a pre-tax basis, ie gross of tax, in accordance with an outcomes reporting standard to be developed by APRA in consultation with ASIC and the industry.

Recommendation 4.8

An outcomes reporting standard should be developed by APRA, after consultation with ASIC and the industry, outlining how investment returns have to be calculated both gross and net of all costs (administration and investment) and taxes and then disclosed only in a format governed by the standard.

Recommendation 4.9

In consultation with industry, government should finalise the details of an investment option performance table for MySuper products and choice investment options, building on the model proposed by the Panel. APRA should then specify this in an outcomes reporting standard. Specifically, the consultation would progress the development of a standardised disclosure format containing:

(a) gross investment returns, costs and investment returns net of all costs (administration and investment) and taxes for investment options for 1, 5, and 10-year periods; and

(b) the number of quarters of negative investment returns the investment option has incurred in the past 10 years, or a proxy figure developed using data published by APRA for those options with a history of less than 10 years.

Recommendation 4.10

Investment option performance table data would have to be maintained by trustees and be easily accessible on the fund's website for as long as the fund remains in existence.

Recommendation 4.11

Trustees of large APRA funds should disclose each diversified investment option's investment return target and risk target, as shown in Figure 4.1 of chapter 4 in a product 'dashboard'. A similar approach should be required for undiversified options, with the underlying asset class or classes being disclosed in place of the 'investment return target'.

Recommendation 4.12

In consultation with industry, APRA should develop an outcomes reporting standard dealing with all of the requirements for the product 'dashboard'. Specifically, the consultation should progress the development of a product 'dashboard' containing the:

(a) net investment return target (after-tax), which should be expressed as a percentage above CPI, over a rolling 10-year period;

(b) range of possible outcomes for a MySuper product or choice investment option (ie risk target) over a 10-year period in a visual, diagrammatic format;

(c) the projected liquidity of the MySuper product or investment option;

(d) projected Total Annual Expense Ratio (TAER) which would capture all the projected costs to at least the first non-associated entity level; and

(e) relative ranking of overall fees (as collected and published by APRA).

Recommendation 4.13

As part of the development of an outcomes reporting standard, APRA, in consultation with the industry, would ensure trustees report costs to APRA on a consistent basis. The standard would prescribe:

(a) 'cost categories' and their composition;

(b) requirement for 'cost categories' to be subject to an annual audit;

(c) 'cost categories' to be reported in the APRA annual return at the whole of fund and MySuper levels; and

(d) costs to be disclosed to at least the first non-associated entity level.

Recommendation 4.14

Trustees offering MySuper products should be required to participate in APRA-approved benchmarking surveys that would measure their relative efficiency against peers in a number of key areas (eg administration costs per member, service standards) in accordance with an outcomes reporting standard to be developed by APRA in consultation with ASIC and the industry. APRA should be required to publish the results of such benchmarking surveys.

Recommendation 4.15

APRA should have explicit powers to collect superannuation fund data on a 'look-through' basis so that it can achieve an understanding of the fund's asset allocation, risk, returns and costs.

Recommendation 4.16

Trustees of large APRA funds should be required to disclose their complete portfolio holdings on a six-monthly basis in accordance with an outcomes reporting standard to be developed by APRA in consultation with ASIC and the industry. This would require disclosure to APRA within 60 days after the end of each six month period, corresponding with normal financial years and half-years, and then public disclosure of the same information, on the fund's website, three months later.

Recommendation 4.17

Trustees of large APRA funds should maintain a website that provides, free of charge, systemic transparency about the fund and the fund's management.

Recommendation 4.18

Trustees should retain the last 10 years' worth of such information and make it available on the fund's website.

Recommendation 4.19

Trustees should be required to publish on the fund website the historical Total Annual Expense Ratio (TAER), which would capture the historical costs to at least the first non-associated entity level, for each MySuper product or choice investment option within the fund.

Recommendation 4.20

Government should task ASIC, in consultation with industry, other regulators and consumer groups, to establish a central website about superannuation to draw together features, including standard disclosure of legislative, tax and other super-related features, and to be a portal to other superannuation-related information. All large APRA funds would be required to link their websites to this site.

10.5 Chapter 5: Insurance in superannuation

Recommendation 5.1

Life insurance cover and TPD cover (where available, depending on occupational and demographic factors) must be offered on an opt-out basis in MySuper products.

Recommendation 5.2

The requirement for a minimum level of life insurance that must be offered by eligible choice funds as set out in Regulation 9A and Schedule 1 to the Superannuation Guarantee (Administration) Regulations 1993 should be repealed.

Recommendation 5.3

Trustees of MySuper products, and trustees of large APRA funds that offer insurance, should have a statutory duty to manage insurance with the sole aim of benefiting members, including:

(a) selecting insurance cover with regard to the cost and value for money for members;

(b) negotiating the terms of the insurance contract, including adequacy of the level of default cover; and

(c) pursuing claims that the insurer has denied in part or in total where there is a reasonable expectation of success.

Recommendation 5.4

The SIS Act should be amended to require trustees of MySuper products, and large APRA funds that offer insurance, to devise and implement an insurance strategy specifying the types of insurance to be offered and the default and permissible maximum levels of cover to be offered.

Recommendation 5.5

APRA should issue guidance material to trustees to help them in developing an insurance strategy.

Recommendation 5.6

In the choice sector, trustees should be allowed to offer life and TPD insurance on an opt-out or opt-in basis, or not at all.

Recommendation 5.7

The Superannuation (Resolution of Complaints) Act 1993 should be amended to allow the SCT to consider complaints in respect of TPD claims when the claim has been lodged with the trustee within six years of the member ceasing employment and the complaint has been made to the SCT within two years of the trustee's decision.

Recommendation 5.8

The SIS Act should be amended so that the trust deed of a large APRA fund is deemed to define total and permanent disablement in the same way as the insurance policy held by the trustee at the relevant time.

Recommendation 5.9

Income protection may be offered on an opt-out or opt-in basis, or not at all by trustees of MySuper or choice funds.

Recommendation 5.10

Apart from life, TPD and income protection insurance, no other type of insurance (for example, trauma insurance) should be permitted to be paid for by members through their superannuation and any existing policies outside those categories should be phased out.

Recommendation 5.11

Trustees of large APRA funds should be required to publish on their websites the terms and conditions applicable to each type of insurance offered by the fund, along with other information relevant to members, including:

(a) a plain English explanation of the policy terms;

(b) premium tables showing the gross premium charged for each category of member (if relevant) at each $1,000 of cover at current age with a standard frequency of payment. Any additional cost associated with the insurance should be noted as part of this disclosure; and

(c) TPD claim success rate on a basis to be determined after consultation with the industry.

Recommendation 5.12

Up-front and trailing commissions and similar payments should be prohibited in respect of any insurance offered to any superannuation entity, including to SMSFs, regardless of rules on commissions that might apply outside superannuation.

Recommendation 5.13

MySuper trustees should pro-actively offer intra-fund advice to members in relation to their insurance in MySuper.

Recommendation 5.14

The SIS Act should be amended so that binding death nominations would be invalidated when certain 'life events' occur in respect of the member. The current systems used by States and Territories under which testamentary dispositions are invalidated could be used as guidance for creating a single national model.

Recommendation 5.15

Subject to recommendation 5.14 being implemented, the SIS Act should be amended so that binding death benefit nominations only have to be reconfirmed every five years.

Recommendation 5.16

After a suitable transition period, self-insurance of any fund benefits, including death and TPD benefits, should not be permitted in any large APRA fund except defined benefit funds (or sub-plans) that are currently allowed to self-insure.

10.6 Chapter 6: Integrity of the system

Recommendation 6.1

New capital requirements for trustees on a risk-weighted basis should be phased-in over time:

(a) the SIS Act should be amended so that the governing rules for all large APRA funds are deemed to include a provision enabling the trustee to maintain a dedicated and identifiable operational risk reserve separate from member account balances;

(b) all large APRA funds must hold a minimum level of operational risk reserve, which reserve cannot be fully offset by trustee capital;

(c) legislation should define a minimum dollar figure for operational risk reserves and a maximum amount, expressed as a percentage of assets in the fund. APRA should have the power to increase the minimum level of capital on a risk-assessed basis. Details of defining a risk-weighted requirement between the minimum and maximum should be developed by APRA in consultation with industry;

(d) should APRA's assessment of risk in the fund lead it to the view that it would be appropriate for the fund to hold a higher level of reserve than the maximum amount set out in legislation, APRA should use other tools available to it to cause the trustee to reduce the risk exposure of the fund;

(e) any capital requirement that would otherwise be imposed under the trustee's Australian financial services licence in respect of non-superannuation business should be in addition to the capital requirement imposed under the SIS Act;

(f) trustees of SAFs should be required to hold an amount of net tangible assets in their own right, calculated by APRA having regard to the operational risk reserve that would be required if the aggregate of SAFs under trusteeship were a single fund; and

(g) the capital adequacy requirements for prudentially-supervised conglomerate groups should have regard to the operational risk reserves in any superannuation fund or funds that are in the group and adequacy requirements for group trustees should have regard to the risk-weighted assets of the rest of the conglomerate group.

Recommendation 6.2

The SIS Act should be amended to:

(a) define 'superannuation administrator' and empower APRA to license superannuation administrators, to impose conditions modelled as appropriate on the conditions applicable to RSE licensees, and to enable APRA to impose, modify or revoke additional conditions. Licence conditions should include a risk-weighted capital requirement;

(b) require that trustees may only use a superannuation administrator licensed by APRA for administration functions which are covered by the outsourcing operating standard. This process should be funded by a levy on those administrators;

(c) require commercial clearing houses to be licensed as administrators; and

(d) make clear that the trustee remains liable to the member in the first instance even if the trustee has outsourced administration to a licensed administrator.

Recommendation 6.3

Obligations imposed by way of licence conditions on external administrators should be replicated where appropriate by variations to the licence conditions of RSE licensees that operate an in-house administration system.

Recommendation 6.4

Section 29PD of the SIS Act should be repealed, so that the trustee is not required to make a copy of the trustee's RMP available to a member or to the employer sponsor in the case of a defined benefit scheme.

Recommendation 6.5

The SIS Act should be amended to provide that, if a trustee makes a formal decision that the RMS fully addresses all risks relevant to one or more of the RSEs under its trusteeship and documents that fact within its RMS, it is not obliged to prepare a separate RMP in relation to the nominated RSE(s).

Recommendation 6.6

The Risk Management Plan should explicitly include a liquidity management component to ensure that trustees identify and manage liquidity risk at both the fund level and the investment option level.

Recommendation 6.7

The exception to the portability rules for illiquid assets should be retained for choice products only, but the member's written consent should no longer be required provided that there is adequate disclosure to the member before they select an illiquid investment option.

Recommendation 6.8

Subject to recommendation 6.7, the current portability rules should be retained for both MySuper and choice products.

Recommendation 6.9

The trustee's RMP should have particular regard to liquidity characteristics of investment options offered to members in the retirement phase.

Recommendation 6.10

APRA should issue a prudential standard that focuses on funding to protect vested benefits and specifies the time period within which a defined benefit fund that is in an unsatisfactory financial position must be restored to a satisfactory financial position, in much the same way that the SIS Act presently addresses insolvency of funds and minimum requisite benefits.

Recommendation 6.11

The SIS Act should be amended so that a defined benefit fund which is technically insolvent should not be allowed to accept SG Act contributions unless the fund actuary and the trustee form the view that it is reasonable to believe that the fund will be restored to solvency within the period prescribed under the SIS Act.

Recommendation 6.12

The definition of 'superannuation contributions' in the Corporations Act should be clarified so that there is no doubt that defined benefit contributions are afforded the same protection as accumulation contributions.

Recommendation 6.13

Defined benefit funds should automatically qualify as 'default' funds for SG Act purposes in respect of the defined benefit provided to members so long as the fund meets the requirements of the SG Act to receive contributions.

Recommendation 6.14

If the defined benefit fund is a hybrid fund, then the MySuper criteria must be met for accumulation members in order for the fund to be accepted as a default fund under the SG Act in respect of those members.

Recommendation 6.15

If a member has both defined benefits and accumulation benefits as part of the defined benefit fund's benefit design, and the accumulation benefit is not necessary to meet the employer's SG Act obligations, then the MySuper criteria do not have to be met in respect of those members.

Recommendation 6.16

Trustees of defined benefit funds (or sub-plans) that are presently allowed to self-insure death and TPD benefits should continue to be allowed to do so.

Recommendation 6.17

In developing investment strategies, trustees should explicitly consider both short and long term risks, consistent with their stated investment horizon. Trustees would not be required to make decisions based on ESG issues but as ESG issues represent one type of long term risk, trustees should consider ESG issues as they think appropriate.

Recommendation 6.18

The government should not mandate that superannuation fund trustees participate in any particular investment class or vehicle, including infrastructure.

10.7 Chapter 7: Retirement

Recommendation 7.1

MySuper products must include one type of income stream product, either through the fund or in conjunction with another provider, so that members can remain in the fund and regard MySuper as a whole of life product. The Government should consult comprehensively with industry before mandating the post-retirement arrangements to apply to MySuper products.

Recommendation 7.2

Trustees should be required to offer intra-fund advice proactively to MySuper members as they approach normal retirement age. Over time, advice should be available on as broad a range as possible of the financial issues that members will face in retirement, subject to the requirements of the sole purpose test. In the near term, advice should address investment allocation and alternative retirement products offered within the fund.

Recommendation 7.3

Trustees should offer intra-fund advice proactively to MySuper members in the retirement phase at periodic intervals.

Recommendation 7.4

Trustees must devise a separate investment strategy for post-retirement members in MySuper products which has regard to the factors as set out in section 52(2)(f) of the SIS Act as well as inflation and longevity risk.

10.8 Chapter 8: Self-managed super solutions

Recommendation 8.1

The current membership limit of four members for a SMSF should not be increased.

Recommendation 8.2

Legislation should be passed to provide the ATO with the power to issue administrative penalties against SMSF trustees on a sliding scale reflecting the seriousness of the breach. The penalties should not be payable from the corpus of the fund, and may be applied jointly or severally against the trustees or trustee directors.

Recommendation 8.3

SIS legislation should be amended to provide the ATO with the power to issue relevant persons with a direction to rectify specified contraventions within a specified reasonable time. A breach of a direction should be a strict liability offence.

Recommendation 8.4

The ATO should be given the power to enforce mandatory education for trustees who have contravened SIS legislation. Such education should be provided by a body (which could include commercial providers) approved by the regulator and would be at the cost of the trustees and not the corpus of the fund.

Recommendation 8.5

The ATO should be given the power to issue binding rulings in relation to SMSFs, subject to the implementation of the Panel's recommendation to restructure the SIS Act in chapter 10 of this report.

Recommendation 8.6

The Government should task ASIC, in consultation with industry and the 'expert advisory panel', to develop the SMSF specialist knowledge component of RG 146, which would focus on increased knowledge and competency with respect to the SIS Act.

Recommendations 8.7

Government should legislate to require advisers to hold an AFSL where they provide advice in relation to the establishment of an SMSF. The accountants' licence exemption should not be replaced by any new exemption or restricted licensing framework.

Recommendation 8.8

Government should:

(a) appoint ASIC as the registration body for approved auditors and give ASIC the power to determine the qualifications (including professional body memberships as appropriate) required for eligibility to be registered, set competency standards, develop and apply a penalty regime including the ability to deregister approved auditors. The registration requirements for approved auditors should be linked to minimum ongoing competency and knowledge standard; and

(b) task the ATO to police the approved auditor standards and enable information to be appropriately shared between ASIC and ATO so as to carry out their roles effectively.

Recommendation 8.9

Subject to the Government implementing recommendation 8.8, ASIC should develop approved auditor independence standards, which auditors must meet as part of their ongoing registration requirements, as outlined in recommendation 8.8.

Recommendation 8.10

The 2007 relaxation of the borrowing provisions and the consumer protection measures that have recently been announced should be reviewed by government in two years' time to ensure that borrowing has not become, and does not look like becoming, a significant focus of superannuation funds.

Recommendation 8.11

Legislation should be passed to require credit providers to collect and provide relevant data to APRA that would enable the RBA to publish statistics on the level of finance being provided to superannuation funds.

Recommendation 8.12

SIS legislation, in relation to SMSFs, should be amended so that:

(a) the 5 per cent IHA investment limit be removed so that no IHA investments would be allowed;

(b) SMSFs with existing IHA investments be provided a five year transition period, in which to convert to a SAF or, alternatively, dispose of their IHA investments. No acquisitions of IHA investments would be permissible during the transition period; and

(c) APRA-regulated funds be exempt from these changes.

Recommendation 8.13

SIS legislation relating to acquisitions and disposals between related parties in SMSFs (but not APRA-regulated funds) should be amended so that, either:

(a) where an underlying market exists, all acquisitions and disposal of assets between SMSFs and related parties must be conducted through that market; or

(b) where an underlying market does not exist, acquisitions or disposals of assets between related parties must be supported by a valuation from a suitably qualified independent valuer.

Recommendation 8.14

SIS legislation, in relation to SMSFs, should be amended so that:

(a) the acquisition of collectables and personal use assets by SMSF trustees be prohibited;

(b) SMSFs that own collectables or personal use assets be provided a five year transition period, in which to convert to a SAF or, alternatively, dispose of those assets. No acquisitions of collectables and personal use assets would be permissible during the transition period; and

(c) APRA-regulated funds be exempted from these changes.

Recommendation 8.15

Government should provide the ATO with a specific mandate to collect and produce SMSF statistics, the details of which be developed in consultation with industry, which provide greater understanding of the SMSF sector and its performance.

Recommendation 8.16

The Government should legislate to require SMSFs to value their assets at net market value.

Recommendation 8.17

The ATO, in consultation with industry, should publish valuation guidelines to ensure consistent and standardised valuation practices.

Recommendation 8.18

Government, after appropriate industry consultation, should amend the Corporations Act to ensure SMSF trustees provide all SMSF members with certain key information on an annual basis.

Recommendation 8.19

Government, after appropriate industry consultation, should amend legislation to remove SMSF trustee administrative burdens that are identified as unnecessary.

Recommendation 8.20

Government should legislate so that:

(a) proof of identity checks be required for all people joining an SMSF, whether they are establishing a new fund or joining an existing fund; and

(b) identification measures should not apply retrospectively except for existing SMSFs wishing to organise rollovers from a large APRA fund.

Recommendation 8.21

The Panel recommends that the SMSF registration process capture the details of the person who has provided advice in relation to the establishment of the SMSF and the service providers who establish the SMSF (if they are different entities). This information should also be available to ASIC to assist in regulating AFSL holders and form part of the risk assessment process for both ASIC and the ATO.

Recommendation 8.22

Controls should be put in place to ensure SMSFs can be neither established with, nor subsequently change their name to, the name of, or a name similar to, an existing large APRA fund and that other naming rules applicable to bodies corporate under the Corporations Act be applied to SMSFs.

Recommendation 8.23

Government should provide a system (Super Fund Lookup or an alternative) to:

(a) provide appropriate SMSF information to large APRA funds (which would include member level details, confirmation that identification of member/trustees has occurred and the SMSFs bank account number) to enable the large APRA fund to verify the details of SMSF membership before processing rollover requests to SMSFs; and

(b) require the large APRA fund, upon appropriate confirmation, to immediately process the request and electronically transfer the rollover to the validated SMSF bank account.

Recommendation 8.24

Legislation should be passed to provide for criminal and civil sanctions to enable the ATO to penalise and discourage illegal early release scheme promoters.

Recommendation 8.25

The Government should amend existing tax laws so that:

(a) amounts illegally early released be taxed at the superannuation non-complying tax rate; and

(b) an additional penalty, based on a sliding scale of penalties that takes into account the individual circumstances, should apply.

Recommendation 8.26

Legislation should be passed so that rollovers to an SMSF be captured as a designated service under the AML/CTF Act.

Recommendation 8.27

The Government should amend the SIS Act so as to automatically deem anything permitted by the SIS Act or a tax act to be permitted by SMSF trust deeds.

Recommendation 8.28

Legislation should be passed so that the covenant requiring separation of fund assets from personal or employer assets, as set out in section 52(2)(d) of SIS, be replicated in a SIS operating standard.

Recommendation 8.29

The Government should amend the investment strategy operating standard so that SMSF trustees are required to consider life and TPD insurance for SMSF members as part of their investment strategy.

10.9 Chapter 9: SuperStream

Recommendation 9.1

Relevant legislation should be amended so that in respect of employees who are members of accumulation funds, an employer must provide to the superannuation fund (or clearing house) its ABN and at least:

(a) on first making a contribution in respect of a particular employee to that fund after the amendment comes into effect, the full name, date of birth, current address, email address (if known), mobile phone number (if known) and TFN of that employee, date of commencement of employment and the amount of the contribution being remitted in respect of that employee;

(b) for each subsequent contribution in respect of each employee, the employee's name, TFN and the amount being contributed for that employee. If the contribution is made via a clearing house, the fund SPIN should also be required;

(c) an employer that fails to meet the data requirements set out in (a) or (b) above becomes liable for an administrative financial penalty payable to the ATO in respect of each employee and each day it fails to meet the obligations. The ATO should have a measure of discretion about collection of the penalty. Alternatively, an employer that fails to meet the standards may be deemed to have failed to meet its SG Act obligations; and

(d) a fund should be prohibited from accepting as a member any person for whom there is not provided sufficient identification data (full name, address and date of birth) to provide a proper preliminary identification, and from accepting any contribution which cannot be reasonably identified as being attributable to a particular member.

Recommendation 9.2

If, after having been provided a reasonable opportunity, the employee fails to provide a TFN or other required details to the employer, the employer's SG Act obligations are satisfied if the employer electronically provides such employee identification details as it has to the ATO together with the requisite contribution. The ATO would then treat the contribution as unclaimed money. On provision of the TFN, the ATO would remit the amount held for that employee to the employer's default superannuation fund, together with the employee's TFN, name, date of birth and, where provided to the ATO, current address, email address and mobile phone number.

Recommendation 9.3

The ATO should establish an employment web page where an employer can both register the tax status of a new employee in lieu of completing the paper TFN declaration and simultaneously advise the fund to which super contributions would be paid. The ATO would then communicate the new member details to the fund electronically.

Recommendation 9.4

APRA should convene a stakeholder group including at least the ATO, employers, payroll providers, super administrators and trustee representatives to devise online forms covering all the common processes between:

(a) the employer and the fund;

(b) the fund and the member; and

(c) different funds, such as occurs with 'rollovers'.

Recommendation 9.5

The Government should be prepared to mandate the use of the forms, unless it is satisfied that there is near universal voluntary uptake.

Recommendation 9.6

The Government should consider imposing a prescribed fee to be paid by the employer to any super fund to which the employer contributes on behalf of a member when the contribution is made other than in electronic form accompanied by sufficient details to adequately identify the member. That is, the fee will only apply if the contribution is paid by non-electronic means (such as by cheque) or if any payment is not linked with adequate member details. In order to give employers and industry time to adapt, such a fee should come into effect after education and an appropriate transition phase.

Recommendation 9.7

A condition of holding a licence to administer superannuation funds should be the capacity to provide e-commerce facilities to employers of all sizes.

Recommendation 9.8

Treasury should convene a working group comprising representatives of relevant segments of the financial sector to devise the process for development of SBR-compatible standards that provide for linked personal and financial data transmission and facilitate related software development. The standards should address transactions between employer and fund, fund and member, and between funds.

Development work should be financed through an industry levy.

All administrators and clearing houses should be required to adopt these standards as a licence condition.

Recommendation 9.9

As a standard licence condition, clearing houses (including administrators offering a clearing house service) should be required to provide linked member and funding data electronically to the fund within two business days of receipt of clean data.

Recommendation 9.10

Having regard to the extended use of personal information proposed in SuperStream, Treasury should be tasked with preparing a Privacy Impact Assessment to help identify and assess any privacy impacts of the 'SuperStream' proposals adopted by the Government.

Recommendation 9.11

Relevant legislation should be amended to permit superannuation fund trustees and their agents to:

(a) use TFNs as a primary search key to link contributions and rollovers with member accounts;

(b) seek confirmation from the ATO in relation to each new member that the quoted TFN is correct;

(c) seek confirmation from the ATO in relation to each requested rollover to a SMSF that the member holding the quoted TFN is a member of that SMSF; and

(d) exchange the TFN with other trustees to identify accounts in multiple funds held by the same individual, and hence permit the trustee of the fund to which contributions are currently being made to invite the member to initiate consolidation of the accounts.

Recommendation 9.12

Necessary legislation should be enacted to permit the trustee to auto-consolidate accounts without prior reference to the member, where multiple accumulation accounts within a single fund share a common TFN and member surname and the multiple accounts have not been established by deliberate elections by the member concerned.

Recommendation 9.13

The ATO should develop electronic means to display all the super funds of which an individual logging on is currently a member. Similarly, the ATO should provide an electronic facility to include all member accounts for which it holds TFN identification.

Recommendation 9.14

To facilitate consolidation of multiple accounts:

(a) **procedures should be established between the ATO and administrators and clearing houses so that when an employer seeks to enrol a new member, the fund administrator (or clearing house if one is used) must validate the TFN provided with the ATO to ensure that it is the number for the individual named; and**

(b) **at the same time, the ATO should be required to check its data base to see whether it holds unclaimed money for that member. If so, it should advise the administrator and transfer the money. The ATO should also determine whether the member has more than one account. If the member has more than one account, the administrator of the new fund should be notified and then determine with the member whether they wish to consolidate their accounts.**

Recommendation 9.15

Relevant legislation should be amended to:

(a) **remove from super funds the current exemption from initial customer identification requirements under the *Anti-Money Laundering and Counter-Terrorism Financing Act 2006* when a member exercises a choice to join that fund, or to roll into that fund the whole or part of a benefit from another fund. Risk-based customer identification would ordinarily be satisfied if the member has provided their TFN to the fund and the trustee has confirmed with the ATO that the TFN is correctly associated with the details for that member or the trustee has confirmation from its own records or another APRA-regulated fund that they have previously provided that level of identification;**

(b) **enable the trustee of an APRA-regulated fund, with the authority of a member, to initiate a rollover of all or part of that member's benefit from another fund as though the member had initiated the request to the exiting fund, without further proof of the member's identity being required;**

(c) **require the trustee of any fund receiving such a request to normally remit the member's balance electronically to the new fund within two clear business days, subject to a capacity for APRA to provide relief from this provision when prudential considerations require it;**

(d) **amend the choice of fund form to make it more user-friendly and to enable the member to tick a box requiring all super accounts to be consolidated, with the nominated APRA-regulated fund to action as above. In view of the greater engagement of most SMSF members, and risks identified in the use of SMSFs for illegal early release of superannuation, this facility should not be extended to the trustees of SMSFs at this stage; and**

(e) **override any provision in the governing rules of any fund with a defined contribution component that would otherwise prevent the consolidation of member accounts.**

Recommendation 9.16

Relevant legislation should be amended so that:

(a) an employer is required to remit salary sacrificed and SG Act contributions no less frequently than it is required to remit a member's after-tax contributions;

(b) the timing of payment of SG Act contributions should be adjusted after SuperStream has been implemented so that SG payments align with employers' payroll cycles;

(c) the employer is required to report on each payslip issued to an employee the amount of superannuation to be paid to the employee's fund, whether SG, salary sacrificed or after tax contributions;

(d) the ATO is specified as the sole regulator generally responsible for compliance with all aspects of superannuation contributions, other than those relating to compliance with industrial awards. APRA should retain responsibility for overseeing the solvency of defined benefit plans and any action needed to restore a DB fund to a satisfactory financial position; and

(e) when an employee makes a complaint that an employer is not meeting its SG Act obligations, the ATO should continue, on a risk-assessed basis, to assess the employer's compliance with its SG Act obligations for all employees in the particular workplace, and not only the complainant.

Recommendation 9.17

The Government should task Treasury with coordinating the initial implementation phase of SuperStream, and with advising on sustainable governance and oversight arrangements for the system into the future.

10.10 Chapter 10: Regulatory settings

Recommendation 10.1

APRA's mandate should be broadened to include the task of overseeing and promoting the efficiency of the funds it regulates and the system in which they operate.

Recommendation 10.2

APRA should be given general standards-making power in relation to superannuation (including prudential matters) in order to address the recommendations in this report and to drive efficiencies in the industry.

Recommendation 10.3

That APRA's mandate be broadened to include the collection and publication of data aimed at the efficiency and outcomes of superannuation funds and research into issues arising from that data to assist trustees in achieving better outcomes for members.

Recommendation 10.4

Legislation should be amended to give APRA an administrative power to impose fines, contestable in a court, as an alternative to criminal prosecution in relation to selected SIS Act provisions.

Recommendation 10.5

The Government should explore with APRA and ASIC ways in which the two regulators can work more closely together in discharging their superannuation mandates, in particular in implementing the Review's recommendations in relation to MySuper and increased efficiency more generally.

Recommendation 10.6

The Government should ensure that the ATO is adequately resourced to continue its existing superannuation responsibilities, including the new functions it will administer under SuperStream and other Panel recommendations.

Recommendation 10.7

The Government should consider arrangements for the Productivity Commission to assess, in relation to the Review's recommendations implemented by the Government, five years after the Government's response to this report:

(a) the implementation and impact of the MySuper regime;

(b) the implementation and impact of the SuperStream changes; and

(c) the functioning of the market for retirement products.

Recommendation 10.8

The Government should have the Productivity Commission assess and advise on possible improvements to the regulatory framework for superannuation five years after the Government response to this report.

Recommendation 10.9

The SIS Act should be amended so that the successor fund transfer test is one of 'no overall disadvantage' rather than 'equivalence'.

Recommendation 10.10

The Federal Court should be given new jurisdiction to determine and facilitate product rationalisation in the superannuation industry where the successor fund transfer regime (as amended by the recommendation made in this Review) still does not fulfil legacy product rationalisation objectives.

Recommendation 10.11

CGT rollover relief should be given to superannuation funds in the terms previously afforded by the *Tax Laws Amendment (2005 Measures No.2) Act 2005* and should be permanently available to the industry.

Recommendation 10.12

New Retirement Savings Accounts should not be allowed to be established after MySuper becomes effective and a mechanism should be considered for facilitating existing RSAs to be transferred to MySuper or other superannuation products.

Recommendation 10.13

New Approved Deposit Funds should not be allowed to be established after MySuper becomes effective and a mechanism should be considered for facilitating existing ADFs to be transferred to MySuper or other superannuation products.

Recommendation 10.14

The Government should legislate to abolish the member protection rules.

Recommendations 10.15

The SIS Act should be amended to create a specific RSE licence class for trustees of ERFs. ERF trustees should be subject to very similar duties as apply to MySuper trustees (bearing in mind the different functions and characteristics of ERFs).

Recommendation 10.16

In order to have ERFs more effectively fulfil their intended function:

(a) The RSE licence for each trustee of an ERF should be subject to the condition that they actively cross match with any active fund seeking the service. All ERF licensees must provide an online facility for people to search for lost super; and

(b) All funds should be required to cross match with ERFs for a new member.

Recommendation 10.17

The name of the SCT should be changed to reflect more appropriately its role. 'Superannuation Appeals Tribunal' is suggested.

Recommendation 10.18

The SIS Act should be re-written and restructured to separate and to identify clearly those provisions that are common for all sectors of the superannuation industry and those provisions that are only applicable to particular sectors under the choice architecture model.

Recommendation 10.19

GEERS should be extended to cover up to three months of unpaid employer SG Act contributions.

ENDNOTES

1 Senator the Hon Nick Sherry, Media Release no. 066, '*Expert Panel and Terms of Reference for Review into the Governance, Efficiency and Structure and Operation of Australia's Superannuation System*', 29 May 2009, <http://ministers.treasury.gov.au>.

2 Senator the Hon Nick Sherry, Media Release no. 066, 'Communiqué of Principles', 28 April 2009, <http://ministers.treasury.gov.au>.

3 On 4 August 2009, the Minister for Financial Services, Superannuation and Corporate Law, Chris Bowen MP, announced the appointment of two additional part-time members of the Review Panel.

4 A trillion dollars is one thousand billion dollars – that is, $1,000,000,000,000. In this report, millions of dollars are shown as $M, billions of dollars are shown as $B and trillions of dollars are shown as $T.

5 Over the period from June 1999 to December 2009, total superannuation assets grew from $411.4B to $1.2 trillion, approximately equal to Australia's gross domestic product. Looked at another way, in December 2009, superannuation assets held by funds were almost half the size of the level of assets held by Australia's banks and other authorised deposit taking institutions and almost as large as the deposits held by Australian residents in Australian banks.

6 Treasury estimate (see appendix C for assumptions).

7 APRA, '*Superannuation Trends*', January 2005, <www.apra.gov.au/Statistics/upload/Superannuation-Trends-PDF.pdf>.

8 Basis for forecasts can be found in the key assumptions underpinning the 25-year scenario in appendix C.

9 Financial System Inquiry Final Report, 1997. For example, recommendation 8 (p 264) concerning disclosure requirements for superannuation and other financial products being 'sufficient to enable a consumer to make an informed decision relating to the financial product.'

10 ABS (2008), '*Adult Literacy and Life Skills Survey, Summary Results, Australia',* Cat no. 4228.0, 9 January 2008, <www.ausstats.abs.gov.au/Ausstats/subscriber.nsf/0/B22A471C221C7BADCA2573CA00207F10/$File/4280_2006%20(reissue).pdf>.

11 Roy Morgan (2010), Superannuation and wealth management in Australia, Report May 2010, pp. 30-31.

12 Roy Morgan (2010), Superannuation and wealth management in Australia, Report May 2010, pp. 47.

13 SuperRatings, '*Submission to the Parliamentary Joint Committee on Corporations and Financial Services*' *Inquiry into the Structure and Operation of the Superannuation Industry*', September 2006; Choice, '*Super in a volatile environment*,' 12 May 2008 www.choice.com.au; The Australia Institute, '*The case for a universal default superannuation fund*,' September 2009; Gallery G., Gallery N., McDougall L.(Queensland University of Technology), '*Don't Judge a Superannuation Default Investment Option by Its Name*,' 19 April 2010 http://treasurer.gov.au/DisplayDocs.aspx?doc=transcripts/2008/007.htm&pageID=004&min=njs&Year=2008&DocType=2; Australian Super, 'Review of AustralianSuper's default investment option,' February 2010.

14 Sunstein, Cass, Administrator of the White House Office of Information & Regulatory Affairs, 17 February 2010 speech entitled '*Humanizing Cost-Benefit Analysis*', http://www.whitehouse.gov/omb/oira_speech_02172010/.

15 Thaler R. H., and Sunstein, C. R., *Nudge: Improving about health, wealth and happiness*, Yale University Press, 2008 and Mitchell, O and Utkus, S, *Pension Design and Structure: New Lessons from Behavioral Finance,* Oxford University Press, 2004.

16 Chant West, *Insurance in Superannuation*, Research Report, May 2010.

17 See ABS, *Employment Arrangements, Retirement and Superannuation, Australia,* April to July 2007.

18 APRA Annual Superannuation Bulletin June 2009 Table 3.

19 *ATO Annual report 2008–09* <www.ato.gov.au/content/downloads/cor00216293AR0809.pdf>.

APPENDICES

APPENDIX A: THE SUPER SYSTEM REVIEW PANEL

1.1 The Panel

The Chair of the Review Panel was Jeremy Cooper. Jeremy was supported by seven part-time panel members: Kevin Casey, Greg Evans, Sandy Grant, Dr David Gruen, Meg Heffron, Ian Martin and Brian Wilson whose summary biographical details are set out below.

Chair

Jeremy Cooper — a former Deputy Chairman of ASIC (2004 — 2009). Prior to that, he was a partner at Blake Dawson, where he worked principally in the area of mergers and acquisitions and corporate advice for 20 years. Mr Cooper has been a member of the Corporations Committee of the Business Law Section of the Law Council of Australia since 1995. Jeremy is a senior fellow of the Financial Services Institute of Australasia (Finsia) and a fellow of the Australian Institute of Company Directors. From 2006 to 2009, he was a member of the Corporations and Markets Advisory Committee, which considers references from the Australian Government on corporate law reform issues. Jeremy is also a member of the Finsia Policy Advisory Council, the Geelong Grammar School Council, and the Industry Advisory Committee of the Australian Centre for Financial Studies. While at ASIC, Mr Cooper had oversight responsibility across a range of ASIC's teams in the financial services sector, including superannuation, financial advisers and consumers and retail investors. Apart from this Review, Mr Cooper has no interest in the superannuation industry other than being, with his wife, a trustee-director and member of their SMSF.

Expert Panel

Kevin Casey — has had more than 40 years experience in the superannuation industry, mainly in the retail superannuation sector. Mr Casey spent 30 years at AMP where he variously managed corporate superannuation relationships, development of superannuation computer systems, superannuation administration procedures and superannuation and technical strategy for AMP's superannuation businesses. Mr Casey also served as Secretary and a director of AMP Superannuation Limited, AMP's public offer trustee and was also a member elected director of the then AMP Officers' Provident Fund. Mr Casey also sat on joint Government/department/industry committees on the development of superannuation legislation, was a member of the Investment and Financial Services Association (IFSA) superannuation committee and the Association of Superannuation Funds (ASFA) post retirement committee and after he left AMP, was CEO of the Australian Retirement Income Streams Association (ARISA) before it merged with IFSA in 2002. Mr Casey is now retired and has his retirement savings in an allocated pension managed by an Industry Fund.

Greg Evans — is the Director of Economics at the Australian Chamber of Commerce and Industry (ACCI). Mr Evans is an economist with a background in both the private and public sector. His early career commenced in the banking sector where he specialised in project finance for infrastructure and resource related projects. Moving to the public sector, he worked for the Commonwealth Department of Finance and was involved in the sale of several government business enterprises. He later joined the Commonwealth Treasury in the international economy division. Mr Evans has subsequently held positions as a ministerial adviser and in various industry associations in the farming and energy sectors. He joined the Australian Chamber of Commerce and Industry in 2004.

He is a director of the International Chamber of Commerce (Australia) and is a member of the Government's Standard Business Reporting board. His superannuation arrangements include a balance held in a public sector fund and he is also a contributing member to an industry superannuation fund.

Sandy Grant — has a superannuation and financial services industry background spanning more than 40 years, mainly, but not exclusively, in the not-for-profit superannuation fund sector. Positions held by Mr Grant include managing director of building industry fund Cbus, managing director of Industry Fund Services and general manager of superannuation administrator, Jacques Martin Industry. Prior to that, Mr Grant held various positions with the Colonial Mutual Group where he began his career. After retiring from full-time work in 2008, Mr Grant served as chair of the policy committee of the AIST until his appointment to the Panel. He is presently a trustee-director of CareSuper, a director of Members Equity Bank (a full-service bank owned by industry super funds), chair of the Members Equity subsidiary Industry Fund Services Pty Ltd, a director of Superpartners Pty Ltd, a superannuation administrator, and a director of Master Builders Victoria Foundation Limited. He is a member of Cbus and CareSuper.

David Gruen — is Deputy Secretary and Executive Director, Macroeconomic Group at the Australian Treasury, which he joined in 2003. Prior to that, Dr Gruen was Head of the Economic Research Department at the Reserve Bank of Australia between 1998 and 2002. He worked at the Reserve Bank for 13 years, in the Economic Analysis and Economic Research Departments. With financial support from a Fulbright Postdoctoral Fellowship, Dr Gruen was visiting lecturer in the Economics Department and the Woodrow Wilson School at Princeton University from 1991 and 1993. Before joining the Reserve Bank, Dr Gruen worked as a research scientist in the Research School of Physical Sciences at the Australian National University and holds PhD degrees in physiology from Cambridge University, England and in economics from the Australian National University. He is a member of the Reserve Bank of Australia's Officers Superannuation Fund, the Public Sector Superannuation Scheme, and Vanguard Personal Superannuation.

Meg Heffron — is a principal and senior actuary of Heffron Pty Ltd, an independent firm which has specialised in providing self-managed superannuation fund services to accountants, financial advisers and trustees since 1998. Prior to establishing Heffron, she was a principal at Mercer Wealth Solutions in the firm's corporate superannuation department and responsible for actuarial and general advice to trustees and employer sponsors of corporate superannuation funds. Meg is a recognised expert on self-managed superannuation fund issues and one of the few actuaries to specialise exclusively in this area. She participates in a range of industry and professional committees including the Small Funds sub-committee of the Institute of Actuaries of Australia and the National Tax Liaison Group (Superannuation) of the Australian Taxation Office. She and her husband have operated their own SMSF since 1997.

Ian Martin — has over 25 years experience in the investment management, superannuation, investment banking and financial services sectors in Australia and internationally. He is a former Managing Director and CEO of the BT Financial Group and Chairman of the Global Investment Management Group of Bankers Trust New York Corporation. He was also the Inaugural Chairman of the Investment and Financial Services Association (IFSA). Prior to joining the private sector, initially as an economist before moving into investment management, Mr Martin spent nine years in various positions with the Australian Treasury. He holds an Honours Degree in Economics from the University of Adelaide, an Advanced Diploma from the Australian Institute of Company Directors, and has completed advanced short courses in investment management at London Business School and Princeton University. He is currently a non-executive director of Argo Investments Limited;

St Vincent's and Mater Health Limited; and Chairman of Sydney's Wayside Chapel Foundation; and has previously been an independent non-executive director of Babcock & Brown Limited and GPT Group. Mr Martin has an SMSF.

Brian Wilson — Mr Wilson has extensive financial services experience, including involvement with both the funds management and investment management sectors. Mr Wilson retired in 2009 as a Managing Director of the global investment bank Lazard, after co-founding the firm in Australia in 2004. His career as an investment banker specialising in corporate financial advice encompassed over 30 years. Prior to joining Lazard, he was a Vice Chairman of Citigroup Australia and its predecessor company Salomon Smith Barney Australia and previously a director and co-head of Investment Banking of Schroders Australia, a principal of Lloyds Corporate Advisory Services and a director of Bank of America Australia. Mr Wilson is also Pro-Chancellor of the University of Technology, Sydney, a non-executive director of Bell Financial Group and a member of the Foreign Investment Review Board. Apart from this Review, Mr Wilson has no interest in the superannuation industry other than as a trustee-director and member of his and his wife's SMSF.

1.2 Panel brief

The Panel was supported by a secretariat drawn from Treasury, the private sector and the regulatory agencies with responsibility for superannuation.

The Panel was asked to examine and analyse the governance, efficiency, structure and operation of Australia's superannuation system, so as to achieve outcomes in the best interests of members and to maximise retirement incomes for Australians. The Review was asked to report to the Government by 30 June 2010.

In announcing the Review, the former Minister for Superannuation and Corporate Law, Senator the Hon Nick Sherry, noted:

> *'The Expert Panel will guide what will be a substantial national project aimed at boosting the retirement savings of all Australians by increasing efficiencies, reducing costs and fees and in turn lifting long-term rates of return'.*[1]

On 6 June 2009, the Hon Chris Bowen MP was appointed the Minister for Financial Services, Superannuation and Corporate Law, and assumed responsibility for the Review.

1.3 Approach to the task

1.3.1 Three-phased consultation process

The Review was divided into three phases:

Phase One — Governance;

Phase Two — Operation and Efficiency;

Phase Three — Structure (including SMSFs).

1 Senator The Hon Nick Sherry, Media Release no. 066, '*Expert Panel and Terms of Reference for Review into the Governance, Efficiency and Structure and Operation of Australia's Superannuation System*', 29 May 2001, <http://ministers.treasury.gov.au>.

More detail about the approach the Panel took to the Review can be found in *The Scope of the Review: A Three-Phased Consultation*.[2]

At the start of each phase, the Panel published an issues paper with a view to helping stakeholders frame their submissions at the appropriate conceptual level.[3] Interested parties had a period of approximately eight to ten weeks to make submissions in response to the themes and issues raised in each issues paper. The Panel then released one or more preliminary report(s) in response to each phase (outlined at 0).

The Panel received over 450 formal submissions, and many more informal submissions, amounting to over 7,300 pages of opinions, ideas and data. Importantly, over 200 of those submissions were made by individual super fund members.

The Panel continued to receive submissions addressing its preliminary recommendations until mid June 2010. These submissions were all considered by the Panel and taken into account in finalising the recommendations.

1.3.2 Stakeholder engagement

The Panel and Secretariat consulted with a range of stakeholders throughout the Review process, attending over 200 meetings.

More specifically, this stakeholder engagement included:

- a two-week overseas study tour visiting major retirement funds, financial institutions, retirement fund experts and academics, regulators and policy-makers in New York City, Pennsylvania, Washington DC, Amsterdam, Stockholm, London and the OECD in Paris;
- consultation with international experts, including discussions with various Canadian pension fund executives and officials from the Chilean Superintendencia de Pensiones;
- consultation with focus groups of super fund members in capital cities and regional centres to better understand the member experience;
- discussions with academic and industry experts, super fund executives, professional services firms, fund managers, investment banks, trustees, industry organisations and regulatory agencies, both in Australia and overseas;
- industry roundtables on topics as diverse as: insurance; administration; advice; DB plans; SMSFs (three roundtables); legal governance (two); member and consumer issues; and on the choice architecture proposals (two);

2 Super System Review, *The Scope of the Review: A Three-Phased Consultation*, 25 August 2009, <www.supersystemreview.gov.au>.

3 Super System Review, *Phase One: Governance*, 25 August 2009, <www.supersystemreview.gov.au/content/downloads/governance_issues_paper/governance_issues_paper.pdf>. Super System Review, *Phase Two: Operation and Efficiency*, 16 October 2009, <www.supersystemreview.gov.au/content/downloads/operation_effiencency_issues_paper/Phase_Two_Operation_and_Efficiency_Issues_Paper.pdf>. Super System Review, *Phase Three: Structure*, 14 December 2009, <www.supersystemreview.gov.au/content/downloads/structure_issues_paper/Phase_3_Structure.pdf>.

- making information about the Review publicly available online: www.supersystemreview.gov.au;
- various newspaper opinion pieces; and
- stimulating public debate through participation and speaking engagements at a range of conferences and seminars.

1.3.3 Preliminary Reports

Prior to this final report, the Panel issued a total of nine preliminary reports and papers, along with a report from Deloitte Actuaries & Consultants about the likely total cost to members of MySuper. The decision to release preliminary reports was made in the interests of transparency and to encourage debate.

Title	Date of release	Content
Scope of the Review: A Three-Phased Consultation	25 August 2009	Set out the Panel's approach to the Review
Phase One Issues Paper — Governance	25 August 2009	Raised issues relevant to governance, to guide interested parties in making submissions
Phase Two Issues Paper — Operation & Efficiency	16 October 2009	Raised issues relevant to operation and efficiency, to guide interested parties in making submissions
A Statistical Summary of Self-Managed Super Funds	10 December 2009	A broad factual overview of the SMSF sector
Phase Three Issues Paper — Structure (including SMSFs)	14 December 2009	Raised issues relevant to structure and SMSFs, to guide interested parties in making submissions
Clearer Super Choices: Matching Governance Solutions	14 December 2009	The phase one preliminary report that outlined a 'choice architecture' for the industry
SuperStream	22 March 2010	The phase two preliminary report addressing 'back office' issues with the superannuation industry
MySuper	19 April 2010	Further detail on an aspect of the choice architecture outlined in the phase one preliminary report
Self-Managed Super Solutions	29 April 2010	The phase three preliminary report discussing SMSFs

The Review also received a number of supplementary submissions in response to the preliminary reports, reflecting the importance that individual members, and industry, attach to the issues addressed by the Review.

APPENDIX B: OVERVIEW OF THE SUPERANNUATION SYSTEM

2.1 Background

The aim of superannuation is to provide a means by which people can save for a dignified retirement. For many years, the age pension was the central means of providing retirement incomes for most Australians. However, while the age pension will provide an essential safety net, superannuation savings holds the key to higher retirement income, for most people.

To ensure that the retirement income policy is fiscally sustainable in the context of an ageing population, Australia has a three-pillar approach. The three pillars are: voluntary superannuation and other private savings; compulsory superannuation savings through the SG Act arrangements; and a means-tested, taxpayer-funded age pension.

2.2 Different superannuation sectors

Superannuation funds are the vehicles for the superannuation system to deliver the intended retirement savings outcomes. APRA divides Australia's superannuation funds into five main segments: corporate, public sector, industry, retail and small funds. The Review uses these classifications for the purposes of this report.

Corporate funds are funds operated for the benefit of employees of a particular company or corporate group.

Industry funds are funds formed to provide access to superannuation for employees working in the same industry, although an increasing number of industry funds are now open to the public.

Public Sector funds are funds that provide benefits for government employees, or are schemes established by a Commonwealth, State or Territory law. There are also Exempt Public Sector Superannuation Schemes which choose not to be regulated by APRA or the SIS Act. However, for statutory purposes, a number of EPSSSs report data to APRA under an agreement between the Commonwealth Government and each of the State and Territory Governments.

Retail funds offer superannuation products on a commercial basis and their trustees are typically a part of a larger financial conglomerate. For APRA's purposes, ERFs are considered to be retail funds.

Small funds are those with less than five members. Almost all small funds are SMSFs, although some are small APRA funds (SAFs).

The following table shows that, at March 2010, corporate funds accounted for 4.8 per cent ($60.9B) of Australia's total superannuation assets, industry funds 18 per cent ($226.6B), public sector funds 14.1 per cent ($177.4B), retail funds 27.9 percent ($351.2B) and small funds 32 per cent ($401.8B).

Table B1: Australia's superannuation industry by entities and assets (as at March 2010)

Sector	Entities	Assets($B)	Market Share of Assets
Corporate	171	60.9	4.8%
Industry	65	226.6	18.0%
Public sector	39	177.4	14.1%
Retail	154	351.2	27.9%
Small funds	426,566	401.8	32.0%
Balance of life office statutory funds	n/a	39.6	3.1%
Total	**426,995**	**1,257.5**	**100.0**

Source: (Quarterly Superannuation Performance, APRA).
Note: Excludes PSTs and single member ADFs.

The table below shows that the number of corporate, industry, public sector and retail superannuation funds has fallen in recent years, reflecting a trend toward consolidation within those sectors of the superannuation industry. This contrasts with continued growth in the number of small funds (almost exclusively SMSFs). The number of small funds has grown steadily, from just over 260,000 entities as at June 2003 to over 410,000 entities as at June 2009.

Table B2: Recent trends in the number of Australian superannuation industry by entities (2003-2009)

Sector	2003	2004	2005	2006	2007	2008	2009
Corporate	1,862	1,405	962	555	287	226	190
Industry	124	106	90	80	72	70	67
Public sector	58	42	43	45	40	40	40
Retail	235	232	228	192	176	169	166
SMSFs	262,175	286,313	303, 004	323,200	361,860	389,308	414,707
Pooled Super Trusts	160	143	130	123	101	90	82
Total number of entities	264,614	288,241	304,457	324,195	362,536	389,903	415,252

Source: (Annual Superannuation Bulletin June 2009, APRA).

Of the 32.7M superannuation accounts covering the Australian population as at June 2009, 0.7M were in corporate funds, 3.1M were in public sector funds, 11.6M were in industry funds, 16.6M were in retail funds (which includes ERFs) and 0.8M were in SMSFs.[4]

In addition to the different types of funds, there are also different types of benefits: defined contribution and defined benefit and a combination of the two called 'hybrid' benefits.

4 APRA 2009 Annual Statistical Bulletin.

Superannuation has become a significant financial asset for many Australians and an important part of the household balance sheet. In August 2009, 88 per cent of all employees had superannuation contributions paid into a superannuation scheme on their behalf by their employer.[5]

It was partly the scale and significance of superannuation that influenced the Government to charge the Panel with the job of reviewing Australia's super system, but also the fact that, despite its growth, there had not been an over-arching review of the current system since its inception in 1993. While there have been other government reviews of aspects of the superannuation system, this is the most comprehensive review so far.[6] As Mercer said in its May 2010 response to the Review's preliminary reports: '*Such a review is long overdue*'.[7]

5 ABS August 2009, *'Employee earnings, benefits and trade union membership*'. Catalogue no. 6310.0, 10 May 2010, <www.ausstats.abs.gov.au/ausstats/subscriber.nsf/0/C61C93BF656DB4C6CA257720001D7CE2/$File/63100_august%202009.pdf>.

6 These have included: Superannuation Working Group, Improving the Safety of Superannuation, March 2002; Productivity Commission, Review of the Superannuation Industry (Supervision) Act 1993 and Certain Other Superannuation Legislation, April 2002; Parliamentary Joint Committee on Corporations and Financial Services, Inquiry into the structure and operation of the superannuation industry, August 2007.

7 *Securing Retirement Incomes: Mercer's response to Cooper's preliminary reports*, May 2010, page 1, http://www.mercer.com.au/referencecontent.htm?idContent=1366410

APPENDIX C: TREASURY ASSUMPTIONS FOR MODELLING

3.1 Key assumptions underpinning the 25-year scenario

A number of assumptions have to be made when making a scenario of the size and structure of the superannuation system in 25 years' time. It is a baseline and does not take account of any changes that might flow from this Review. However, it does take account of recent government policy changes to phase in increases to the SG contribution to 12 per cent by 2020 and for the government to co-contribute up to $500 annually for members on incomes up to $37,000. The key assumptions underlying the forecast are:

- All real forecasts have been calculated using 2009 as the base year with the CPI increasing 2.5 per cent per annum thereafter.
- In real terms, total superannuation assets are assumed to grow at an annual average of about 4.3 per cent from around $1.08T in 2009 to about $3.2T in 2035. Small funds, including SMSFs and small APRA funds, will grow to slightly more than a third of total superannuation assets.
- The number of superannuation funds is expected to continue to decline as funds consolidate. The number of APRA-regulated superannuation funds will reduce from 447, excluding ERFs, in 2009 to 74 in 2035.
- The number of industry funds and retail funds will continue to decline at the same average rate (around 7 per cent per annum) as they have since 1996.
- The number of public sector funds will decline at 2 per cent per annum, the average rate experienced since 1996, excluding the two outlier years experienced after the introduction of the APRA registrable superannuation entity licensing requirements, which saw a large reduction in corporate funds.
- The number of corporate funds has declined, on average, by 20 per cent each year from 1996 to 2009. It is projected this rate of decline will gradually slow.

3.2 Key assumptions in projecting benefit to members of MySuper

The MySuper reforms would have both short-term and long-term impacts on fees as the superannuation industry fully adjusts to the reforms. The direct effect would be to benefit those people who are currently in a MySuper-equivalent product who would have access to lower fees. These are the people who are currently in the default investment option of default funds. As at March 2010, Treasury estimates that there were approximately $560B of assets in default funds, with around $340B of that amount in the default investment option.[8] Treasury estimates an average fee for these assets is 97 bps, based on the Rice Warner *Superannuation Fee Report 2008*.

8 Based on Rice Warner Superannuation Fee Report 2008, APRA 2009 Annual Statistical Bulletin and APRA March 2009 Quarterly Superannuation Performance.

MySuper would also affect other members indirectly. As members could switch between products, it is expected that a lower price for MySuper products would lead to members switching into that product or fees charged in other segments falling (for example, due to consolidation occurring in 'choice' products). This switching would be supported by the new financial advice rules which will require planners to put members' interests above their own and hence the lower fees expected in MySuper would need to be taken into account by planners in making recommendations to members. In addition, there is already some evidence that large financial institutions are more actively marketing lower cost, MySuper-style products. The SuperStream reforms would also help facilitate people switching by making portability easier.

For the purpose of this analysis, it is assumed that the only indirect impact would be members switching to MySuper products, rather than fees for choice products falling.

Given the uncertainty over the regulatory and market reaction to MySuper, these estimates are only broadly indicative. There has been no quantification of costs for ongoing or transitional costs of funds meeting the new MySuper requirements. It is also assumed that fees otherwise remain at their current levels as a percentage of assets.

3.2.1 Short-run impact

Funds would need to consider whether they wished to offer a MySuper product and whether they had the scale to optimise net benefits to members to ensure that they receive an APRA MySuper licence. It is assumed that funds would price their product in the short run, on average, at around 85 bps (all up) for an account balance of $25,000, with a similar investment style as would currently be the case. Based on the Deloitte report, *Default fund costs under the MySuper proposal*, this would be consistent with an average asset size of around $5B, which is around one-sixtieth of the existing overall default option pool. It is assumed that people currently paying for advice in default products would, under MySuper, rely on intra-fund advice that is already factored into the Deloitte MySuper fee.

Based on default assets of $340B, this suggests the initial direct impact could be a saving of about $400M per year from reduced fees in existing default investment options that convert to the MySuper framework.

The indirect impact would depend on the impact of MySuper on fee differentials and the propensity of members to move from the choice and SMSF sectors to the MySuper sector. Treasury assumes in its modelling that there is no movement from retirement income stream products, including SMSFs in the pension phase, into MySuper products. This leaves around $725B of assets in the accumulation phase in SMSFs and the choice sector. Treasury estimates the average fee for these assets is around 128 bps — a differential of 31 bps compared to existing default fund fees. Assuming average MySuper fees fall initially to around 85 bps, the differential would be around 43 bps.

Switching rates between super fund products are currently low. However, the new financial advice reforms and the expected public awareness of the introduction of MySuper could increase the switching rate (that is, there could be a one-off switching rate boost). Treasury assumes 5 per cent of assets (around $35B) are switched to MySuper products in the short run, saving around $150M per year in fees. The combined direct and indirect annual savings in the short term therefore could be around $550M.

3.2.2 Long-run impact

The MySuper reforms would have a larger impact over time as the superannuation system fully adjusts to the reforms. MySuper members will benefit from even lower fees as MySuper funds fully exploit the benefits from economies of scale. Deloitte estimate an average fee (including intra-fund advice) of around 66 bps is achievable on large scale ($20B plus assets) MySuper products. It is assumed that these scale benefits are fully achieved across MySuper products, yielding an aggregate saving of over $1B per year on existing MySuper-comparable assets.

The indirect impact would also be greater in the long run because: (a) the incentive to switch would be higher as MySuper fees fall as scale increases; (b) members who might have initially not switched decide to switch; and (c) members who previously would have moved into the choice and SMSF segments decide to remain in the lower fee MySuper products. In other words, there would continue to be some switch in the stock of funds into MySuper and the flow of funds into the choice and SMSF sectors would slow.

Obviously in the longer run, there will also be more assets in the whole system. However, to simplify comparability, the long-run impact is estimated on the existing size of the superannuation industry. It is assumed the long-run switching rate would be around 15 per cent, that is, around $110B of assets would move to the MySuper segment. (This is consistent with the long-run proportion of assets in default investment options increasing from around 32 to 42 per cent (excluding pension products). Given the fee differential, this equates to a saving of around $700M. The combined direct and indirect impacts could therefore be around $1.7B per year.

3.3 Key assumptions in projecting benefits of SuperStream

The impact of SuperStream would directly reduce the fees of APRA-regulated funds which hold assets of about $860B by reducing operating costs including administration. Treasury estimates that current operating costs of APRA-regulated funds are approximately $4.1B per year or 48 bps per year, based on the Rice Warner *Superannuation Fee Report 2008*.

Several submissions[9] estimate that SuperStream reforms would reduce operating costs in the current system by up to $1B per year and Treasury has used this estimate in its assumptions. Operating costs are expected to reduce because of a combination of innovative technology (such as automated administration and the use of TFNs), stakeholder connectivity, straight through processes, broader industry collaboration on administration functions and fund consolidation.

Treasury has not independently verified these cost reduction estimates. It should also be noted that there would be some upfront costs required by funds to implement SuperStream, such as adjustment of IT systems to meet the new data standards. These have not been estimated though it is expected that the ongoing costs will be relatively small compared to the benefits.

9 For example, Ernst & Young, Submission no. 136, page 8; BT Financial Group, Submission no. 151, page 5; and SuperChoice, Submission no. 189, page 27.

3.4 Impact on typical member

The impact on a typical member has been based on a person on average weekly ordinary time earnings (AWOTE)[10] over a 37 year working life who pays all up annual fees of 97 bps which is estimated to be the current average default investment option fee. In the long run, it is assumed, consistent with the above aggregate analysis, that this member would pay a fee of around 59 bps, as follows:

- MySuper products (with assets of $20B) being delivered for 66 bps (excluding the impact of SuperStream, as estimated by Deloitte; and
- SuperStream delivering savings of around a further 7 bps to the average member in a MySuper fund.

Treasury estimates indicate that this presently represents around a 40 per cent fee cut, lifting the representative member's final superannuation balance by around $40,000 or 7 per cent.

10 ABS (2010), *Average Weekly Earnings*, Cat. 6302.0, February 2010.

APPENDIX D: DELOITTE REPORT

DEFAULT FUND COSTS UNDER THE MYSUPER PROPOSALS

Deloitte.

Super System Review

Default Fund costs under the MySuper proposals

19 April 2010

Contents

1 MySuper: the context for this report

This report details the results of our investigations into the projected costs of a large default superannuation fund established within the MySuper proposals currently being considered by the Review. The basis for this report was a draft discussion paper "MySuper: Optimising Australian superannuation". While this might differ from the Review's final recommendations we are advised that the key aspects of this paper (the Paper) that we mention in this report as influencing our conclusions remain valid.

Our brief

The scope of this report is described in an Official Work Order, which asked us to analyse the projected costs that a large default superannuation fund could charge for an average member with an account balance of $25,000 and for other account balances, assuming a number of investment strategies including:

- A typical balanced asset allocation;
- A defensive asset allocation;
- Use of alternative investments.

We are also asked to comment on the levers and variables involved.

The aim is not to provide definitive conclusions on the actual cost that might apply within a default fund but rather to provide information which can then be used by the Review for informed discussions with the industry.

1.1 This report

The results we present must necessarily be considered within the context implied by the MySuper proposals and we include in this report a brief description of those key features in the Paper most significant in determining costs.

It is widely recognised that there is a lack of quality and consistent data throughout the superannuation industry in Australia. It is not easy for individual Australians, let alone experienced industry practitioners, to compare and contrast performance and costs of funds. We describe the approach we have taken in arriving at the costs presented in this report and the data sources that we have used.

In broad terms we have chosen to subdivide costs into:

- Investment related costs; and
- Operating costs which include any fees paid to third party administrators where they are used as well as the cost of intra-fund advice.

It is our view that investment related costs should be related to the quantum of funds under management and should therefore be expressed as a percentage of assets. Operating costs however, are more correctly related to the number of members and we have, therefore, chosen to express these as a $ cost per member per annum.

All costs quoted in this report exclude any bundled advice and distribution costs as mandated under the MySuper proposals.

We have not taken into account the potential impact of SuperStream proposals in this report.

1.2 No single national default fund

The Paper states that every existing superannuation fund will be able to establish, within its current structures, a MySuper product. There will be no single national default fund but rather the opportunity for all existing superannuation funds to offer a MySuper product.

The Panel is conscious that the overwhelming majority of Australians find themselves in the default investment option of whichever superannuation arrangement they are in. Moreover, for many Australians the fund that they are members of is simply the "default fund" that applies to them because of their current employment or employer.

The Paper proposes that only a MySuper product will be able to qualify as a default fund and that any MySuper product can be nominated as a default fund under award or by an employer.

The Paper therefore anticipates a future where, as today, there are a significant number of default (MySuper) funds of different shapes and sizes.

Defined benefits are explicitly excluded from the MySuper proposals and from this report.

1.3 MySuper: conditions attaching

The Paper states that MySuper is predicated on providing a simple, cost-effective product with a diversified portfolio of investments for the vast majority of Australian workers who are invested in the default option in their current fund.

It is expected that the MySuper product offered by existing funds will essentially be based on their existing default investment option. While this does not require establishment of a separate pool of assets the Paper describes conditions that must be satisfied to qualify as a MySuper product.

These include:

- Separate accounting and reporting;
- Streamlined member reporting and disclosures;
- An obligation to accept all types of contributions;
- A single investment option is to be offered;
- Limits to cross-subsidies;
- Exclusion of bundled advice, but access to general and intra-fund advice in accordance with ASIC RG 200;
- No trailing commissions or ongoing advice payments;
- Basic insurance can be offered but with no commission or like payments;
- Certain requirements surrounding fees:
    - No entry fees
    - Buy/sell spreads demonstrably linked to costs
    - No non-explicit discounts and no rebates
    - Any performance-based fees must comply with Performance Fee Standards to be developed by the Panel in consultation with the industry.

The description above is not comprehensive but rather focuses on points relevant to this report.

1.4 Costs to be balanced against member benefit

The Paper expresses the objective of MySuper to be the availability of a low-cost, no-frills, base superannuation option to all Australians. In emphasising the importance of containing costs the Paper recognises the impact that costs have on the build up of retirement benefits. However, the Paper does not adopt cost as the only, or indeed the most important, measure of product quality.

To the contrary, it explicitly acknowledges that trustees can and will take decisions on behalf of members that increase costs because in their view the end result will be better outcomes for members. It is not hard to describe some such decisions: the view that a "higher cost" balanced investment strategy is better for members than a "lower cost" conservative strategy; the appointment of investment managers at a higher fee than others because of an informed view that they will produce higher net (after fees) returns.

MySuper takes the view that this is not only acceptable but a trustee obligation. The Review, however, seeks to impose greater transparency and accountability on trustees for those decisions.

This is an important point because if cost was the sole criterion then MySuper would encourage trustees to invest assets passively at dramatically lower costs. We know that some funds already invest part of their assets this way. However, the majority do not and many funds firmly believe that they can point to a track record where active investment management, albeit at a higher fee, has produced positive long-term added value for their members.

1.5 MySuper: key points

MySuper, therefore, builds on what exists today and it is expected that the core default investment options of any particular existing funds could form the basis for a MySuper product should they decide to offer one.

To qualify as a MySuper product it must meet certain standards regarding reporting and trustee duties and not include any bundled advice or distribution costs.

This has implications for the costs that we will initially see in MySuper products.

1. On the operations side, the starting position is existing systems and costs. MySuper will include intra-fund advice which will demand much more than a simple record keeping capability. Indeed much of the functionality associated with Choice and highly engaged members will need to be retained. We expect a single operational infrastructure serving all fund members (MySuper and Choice) and only relatively minor segregation of costs between the two.

   Provided that bundled advice and distribution is excluded, we can expect MySuper operating costs to be at or about current costs.

2. Investment costs range widely and depend on some basic trustee decisions including investment style, asset allocation and performance/risk objectives. Consequently, the estimates in this report should not be viewed as being exact and absolute. Instead we present projected costs for a range of basic trustee decisions. These costs represent a baseline with trustees always able to incur higher cost if they believe that in so doing they will generate sufficient extra net return to benefit their membership.

   Significantly, it will remain possible for funds to pool the buying power of all their members, MySuper and Choice both, in purchasing assets. Otherwise costs might increase due to loss of scale.

2 Data

The quality and quantity of publicly available data on the superannuation industry has not kept pace with the growth of the industry.

The lack of standard (and mandatory) reporting templates means that it is very difficult to compare cost structures between funds, between industry sectors and over time. This is true of fees, costs and profit margins earned by those who are providing services to the industry.

Costs are particularly difficult to assess because the annual reports of superannuation funds typically:

- Only record a small component of total investment related expenses; and
- Aggregate other expenses into a single amount which may or may not be described in the notes.

Proprietary data does exist within a number of research houses but is rarely comprehensive or readily comparable across the entire industry.

2.1 Sources of data

For this report we have relied on data that is available publicly, available from deep analysis of publicly available information, and from a range of internal research projects undertaken by Deloitte into the industry, together with the superannuation experience of our practitioners.

One research project is particularly relevant to this report.

Research into costs

In 2008, we undertook research to determine whether there existed scale economies and benefits within the Australian superannuation industry.

At that time we deliberately chose to limit our research to Australian Industry Funds.

There were a number of reasons for this but most relevant to this exercise was that the Industry Funds offered better access to data in that the funds themselves produce financial statements, which are by and large independent of related entities.

Our research examined:

- Annual reports to members, and where available, full financial statements for the fund. These were examined to reveal total operating costs as well as any additional (usually internal) investment costs incurred by the fund.
- The PDS for the default option, which allowed us to identify investment related costs deducted from the return (or unit price) delivered to members. The PDS also provided us with a statement of all member fees which then allowed us to calibrate fees against costs.
- Total fund statistics in terms of the number of members and assets under management to give measures of scale. This was easier to establish within an industry fund context as institutional operations have a number of products, and funds with infrastructure applied across them all.

For this report we have updated this research to allow for the impact of inflation.

More recently, we also surveyed a small number of large Australian superannuation funds across all sectors to gain insights into their responses to intra-fund advice.

The funds surveyed have a combined membership of some 5 million members and, to that extent, offer a reliable view of how the industry might deliver cost-effective advice to members. The responses to this survey, together with a significant amount of additional work we have undertaken over the past six months, gives us the ability to estimate the range of costs at which intra-fund advice could be delivered to members.

3 Describing costs

Set out below is a brief description of the approach that we have taken in presenting costs in this report. In particular it has become common in Australia to express total superannuation costs as a single statistic -- the MER for a fund. This equates all costs to a single % of assets.

However, this disconnects non investment costs from the factors that primarily influence them. Moreover, where such fees are paid to third parties and linked to a growing body of assets it builds in cost escalation.

Investment related costs are quite properly related to the assets under management. We would expect, other things equal, that the quantum of these costs would increase in broad proportion to the amount of assets.

Administration and operating costs are another matter. Many of these costs are transaction -based, while some are fixed. Fundamentally, we would expect that the larger the number of members, the greater the quantum of these costs. In this report we first present operating costs as an annual $ amount per member.

But industry practice is entrenched. These costs are also expressed as a % of assets.

To assist in comparison, when we aggregate all costs (investment plus operating) we do express total costs as a % of assets.

3.1 Investment costs

Investment costs come in a variety of forms and are heavily dependent on the way in which assets are managed and the type of asset held.

Scale influences structure

Smaller funds are less likely to be able to justify an internal investment staff. They will rely more on external advice, support and execution, with trustees and the secretariat devoting some of their time to investment matters. The Australian market place offers assistance in many ways.

As funds grow they approach a size where they can increasingly complement external assistance with internal skills and resources.

It is the overwhelming common practice in Australia for (all but the largest) funds to outsource stock selection decisions to external fund managers in the major asset classes. More recently and with the increase in the use of alternatives we have seen a number of funds also build up portfolios acquired directly, though selected with external advice and assistance.

Some of the larger funds have developed quite an extensive internal investment capability that assumes responsibility for managing a portion of fund assets as well as external supplier relationships, with a range of fund managers.

The size of superannuation funds in Australia is not large by global standards. The simple reality is that many do not have the capacity to put in place specialist internal investment skills and must rely on advice and assistance from third parties.

The asset consultants in Australia occupy a very important and influential position in determining where and how money is invested.

Implemented consultants

As a result of the above we have seen in Australia the rise of what are known within the industry as "implemented consultants". These are organisations which offer a “one-stop-shop” packaged investment capability to those funds that are unable to in-source some or all of the capabilities essential for investment management.

In their simplest form the implemented consultants deliver a service which includes:

- Asset allocation and portfolio construction advice and product;
- Manager research and selection;
- Ongoing monitoring of manager performance and consequent hiring/firing;
- Access to a range of diversified multi-manager portfolios, which typically include a balanced and a conservative option;
- Access to a range of multi-manager sector specific portfolios. Almost always these include the major domestic and international asset classes, and more recently have been extended into alternatives;
- The security afforded by the custodial arrangements put in place by the implemented consultants; and
- The ability to leverage off investment education materials developed by the implemented consultants and made available to their clients.

The implemented consultants operate in a very competitive market and we can draw on a large amount of data in estimating the cost to a fund of retaining their services. This is not intended to be a recommendation to use their services but rather recognises that implemented consultants do offer small to medium funds access to scale that is otherwise unavailable within the funds themselves.

Importantly, the fee charged by implemented consultants includes both:

- The consultants own costs for research, staff and a profit margin; as well as
- The fees that they pay to the managers that they appoint, which include margins for those managers.

From the fund’s viewpoint the fees charged by the implemented consultant are regarded as a cost.

In this report we use the implemented consultant offerings as a proxy for active investment management for funds up to $2 billion in assets.

This figure is a little arbitrary and in our view is still a little below the (cost) breakeven point beyond which it would be possible for a fund to be able to actively manage diversified multi-manager portfolios via direct mandate.

Beyond $5 billion in assets we seek to estimate costs for active investment through a combination of an internal (to the fund) investment function and use of external managers appointed to fund specific mandates.

Active & passive investment

The alternative to active investment is passive or indexed investment. This is more popular overseas than in Australia but there are a number of specialist providers active in the Australian market.

Passive investment is much cheaper than active investment. Very large funds can invest in the major asset classes at close to “nil cost” and effectively capture market returns. It is also accessible to investors at all size points, including individuals. It can be achieved by physically holding assets and regularly rebalancing them or, at an even lower cost, through synthetic instruments.

Our decision to include passive investment in the analysis does not imply any statement from us on the pros and cons of active versus passive. Rather, it is a fact that funds can invest passively at much lower cost.

A decision to invest actively at a higher fee is, therefore, justified in the belief that to do so will generate extra return that more than offsets the additional cost. In fact, the bulk of superannuation assets in Australia are actively invested and many believe they can point to a track record of active management delivering added value.

In this report we show costs for both active and passive investment management.

Asset allocation

The other major factor influencing investment cost is asset allocation.

In this report we produce estimates for a Balanced as well as a Conservative investment portfolio.

We include two sets of calculations.

- For the first we construct a Balanced and a Conservative portfolio excluding some of the more costly alternative asset classes.
- For the second we then recalculate these estimates including some exposure to alternative assets.

We have chosen to build portfolio costs up from costs identified for each asset class. The portfolio costs are simply the weighted sum of the portfolio components. The asset allocation is shown for each portfolio.

Performance fees

We have noted the requirement that performance based fees only be permitted within MySuper products if they satisfy as yet unspecified conditions.

Performance fees in asset management have grown dramatically to the point where they sometimes exceed base fees within a given asset class and can be a material component of total manager fees within diversified portfolios.

The costs presented in this report are based on data, some of which might include an element of performance fees. We are not overly concerned with this. While it might result in our overstating MySuper costs to some extent, performance based fees are not prohibited in MySuper; they are only subject to conditions that are not yet known.

It is also widely known that there is increased scrutiny of performance fees in the wake of the Global Financial Crisis and some funds have openly spoken about acting to contain them.

Presentation of investment costs

In summary, we present estimated investment costs in this report in a way which allow comparisons to be made between:

- Active versus passive;
- Balanced and Conservative asset allocations;
- No exposure to alternatives or some exposure; and for
- Funds of varying sizes.

3.2 Operating costs

It should be possible to analyse operating costs, in total and in segments, within a superannuation fund as is done in other businesses. Unfortunately the data needed is not widely available.

We have been able to estimate total operating (i.e. all non-investment related) costs from our research and also from the annual statements of funds that do not have commissions, like payments, or the cost of extensive comprehensive advice on their P&L statements.

The research did not include funds that paid commissions or where platform fees were paid.

Some funds do include the cost of some elements of advice. Some large funds have internal planners but the cost increment when spread over all members is low (because of low take-up). Some smaller funds capture elements of intra-fund advice from their third party administrator and to this extent the costs we report are a little higher than they would otherwise be. Thus total operating cost has become our starting point.

We have drawn on other available sources, including our tender work, to estimate the costs that a third party administrator would charge funds of varying size. In doing this we have been aware that when administration is bundled with other services (especially asset management) it can be used as a loss leader. Moreover, the range of services provided under the generic label of administration varies widely and often include items that fall within what the Review has termed “bells and whistles”. It is impossible to extract these out. Again, the effect is to slightly overstate fees charged by the third party administrators for a strict “no frills” administration service. However, we do not believe this is material.

Internal “trustee office” costs are the difference between the two.

We believe that we can reliably estimate the fees in the market. Moreover, those fees would be inclusive of profit to the provider at levels consistent with current industry practice.

3.3 Intra-fund advice

Our research indicates that the provision of personal advice (including intra-fund advice) is currently a major issue across all sections of the industry. Much thought and effort is going into how this can be delivered en-masse to members at low cost. For some this means identifying gaps in operational infrastructure and working out how to fill it. For others it means promoting capabilities that have been dormant in the past. For some it may mean radically rethinking operating structures and partners.

The reality is that intra-fund advice is in its infancy. It has not been widespread in the past. Most funds have hitherto restricted themselves to providing general information and in exceptional cases escalating contact via telephone for more complex queries. Some have introduced an ability to deliver a Statement of Advice in certain circumstances but use of this latter facility has not been widespread.

The significance of this is that an analysis of past costs will not include a significant component attributable to advice.

MySuper makes provision of intra-fund advice compulsory but envisages that it will be spread across the entire membership which will clearly add to costs.

The following graphic seeks to simply describe the “advice continuum” as this is central to the way in which we have sought to allow for intra-fund advice in this report.

Basic information	From knowledge to understanding	General assistance	Assistance on specific matters	More complex advice but still restricted to matters within the fund	Full comprehensive financial advice
The member should know what their current interest is	But what does this mean. The member should understand their benefits, entitlements and rights	The member is provided with general information that they may or may not use to assist them in structuring their participation in the fund.	The member is offered clearly defined or scoped assistance/advice on a particular matter – as it applies to the member. Commonly a single issue such as insurance, contributions, salary sacrifice	This is all about assisting the member as far as is possible in helping the member capture full value from their participation in the fund – as it applies to the member. It does not extend to matters beyond the fund and needs must be suitably qualified	Some need it, but at specific times

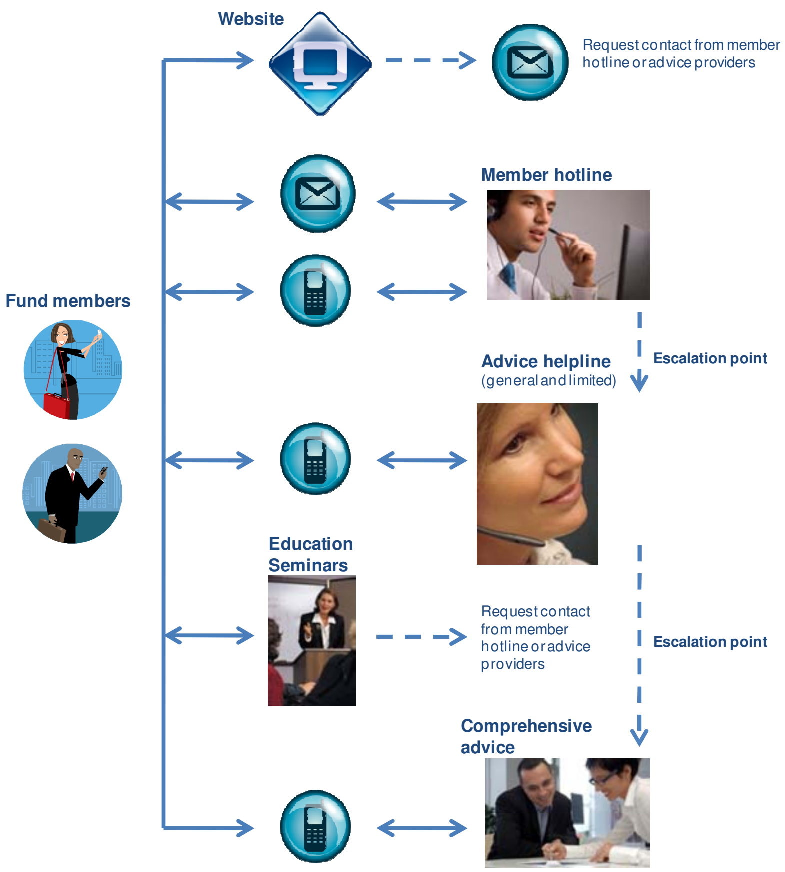
Most funds already provide assistance ranging between basic information and through to some form of general assistance. They do this through written material, statutory disclosures, tools on the website, and response to phone queries. Importantly, provided demand is manageable, the cost is (and can be) met from existing infrastructure.

Comprehensive financial advice usually involves face to face contact with a professional adviser. As such it is labour intensive and involves a significant cost. Some funds do offer this, but those funds upon which we have based our costs do so to a very limited extent, and of these many charge the individual member an additional fee for service. Our understanding is that a MySuper product will not package full comprehensive advice within its standard fee, though the members would be able to access this service on a user pays basis.

What remains is member specific assistance/advice on either a single issue or on a more complex matter, but in respect of matters relating to participation in the fund, as the areas that will generate the bulk of additional operating costs associated with intra-fund advice.

The cost of intra-fund advice depends on both the demand for this and the cost of delivery in each case. It is fair to say that a number of organisations are gearing up to provide third party services, linking into the existing administrative infrastructure of funds. Indeed, this is essential in order to provide the service cost effectively. In some cases there will be a need to materially upgrade administration system functionality, reliability and the training given to people in contact with members - but this is not a bad thing in itself.

A major challenge for funds is to efficiently put those seeking intra fund advice in touch with appropriately qualified people. The graphic below illustrates the process envisaged, as well as showing how delivery of intra-fund advice is intertwined with the administrative infrastructure of any fund. The better administration platforms are able to rapidly deploy existing (though latent) intra-fund advice capability without significant transition cost.



3.4 Insurance & insured benefits

It is proposed that MySuper products will be able to offer certain insured benefits and the Panel has asked the industry to respond with its views on what should and should not be permitted.

The reality is that insurance premiums and related costs constitute one of the largest items of expenditure of superannuation funds. Despite this we have decided that it would be inappropriate to include premiums as a cost item in this report because premiums for individuals vary according to the risk, amount of cover, and the type of benefit. At a fund wide level the total premium is highly dependent on the fund's demographic profile.

We adopt the view that an insurance contract for services and benefits is entered into between the trustee acting on behalf of members and the insurance company and should be assessed separately to other aspects of the fund's operations.

3.5 Costs & profit

Costs paid by a fund, or a MySuper product, to an unrelated third party service provider will include an unspecified profit margin to the provider.

Consequently, many of the costs that are cited in this report include service provider profit margin.

3.6 Uncertainty in costs quoted

In this report we present projected costs in a series of tables, expressed as either a % of assets under management or as an annual cost per member. We believe that the costs are reasonable, achievable and offer a realistic picture of what might be incurred within a no-frills MySuper product.

We have also described the process by which we have arrived at these numbers and it should be apparent that there is some element of approximation and estimation inherent in their calculation. The cost estimates presented should be regarded as being representative of a range of costs, anywhere within which it would be reasonable to expect that a MySuper product costs could lie.

4 Investment costs

Investment costs across the superannuation industry range broadly. It is impossible to generalise and any statement of costs must necessarily be presented within the context of:

- Whether the assets are managed actively or passively;
- The underlying asset allocation;
- The extent to which the trustee has decided to invest in alternative and illiquid assets in an effort to capture the benefits of diversification and the returns available in those asset classes;
- Scale.

4.1 Passive investment

Those who advocate passive investment contend that over the long term it is difficult to outperform the market and that investors should simply aim for market returns within a given asset class, minimise fees and devote attention to asset allocation which is responsible for the bulk of actual return.

In any case, the fact is that fees paid for passive management in the major asset classes are significantly less than for otherwise equivalent active management. Consequently, if we desire to illustrate how low asset management fees can be, then our starting point is passive management. Importantly, passive management is readily accessible by all Australian superannuation funds and individuals, if so desired.

Cost numbers

The following table shows estimates of costs for passive investment for funds of varying sizes.

Cost of investing passively (Basis points)									
Asset class	Asset allocation		Total MySuper fund asset size $ millions						
	Balanced 70/30	Defensive 30/70	<100	500	1,000	2,000	5,000	10,000	>20,000
Aust shares	30%	15%	25	15	10	5	4	2	1
Int'l shares	25%	15%	28	17	13	8	4	2	1
Emerging markets	5%	0%	70	55	45	30	22	16	8
Aust listed property	5%	0%	30	15	10	5	2	1	1
Global listed property	5%	0%	50	45	16	8	4	2	1
Aust FI	15%	35%	15	6	5	4	3	2	1
Int'l FI	10%	25%	25	10	8	6	4	2	1
Cash	5%	10%	10	5	5	3	1	<1	<1
Custody Costs**			4	4	4	3	2	1	<1
Overall portfolio cost (Basis points)									
Balanced option (70/30)*			31	21	16	10	7	4	2
Conservative option (30/70)*			24	14	12	8	5	3	2

* *Numbers shown should be viewed as centred within a range extending ±1-2 basis points*

** *Where the fund holds the assets via a mandate with the investment manager, otherwise close to zero.*

Comment

The costs quoted involve a direct relationship with the supplier of the passive products. We know that some funds offer passive options in the major asset classes as part of a broader investment menu. This allows individuals to select them if they choose to. Prices can vary widely.

We have not included Exchange Traded Funds in our analysis. These are readily available at costs lower than shown above.

It could be justifiably argued that a fund, no matter how small, will devote some internal resources to investment management. It will at least require access to some independent advice in arriving at a decision to invest passively, in deciding on the asset allocation/investment strategy and in deciding the organisation to appoint. Thereafter, it must necessarily monitor performance and periodically reassess the appropriateness of the arrangements in place.

This is undoubtedly true, and those costs would be in addition to those shown.

That said:

- It is our experience that a smaller fund would make key strategic decisions with external advice and then delegate broadly to the investment managers appointed. Performance would be monitored by the trustee and its secretariat, without a dedicated investment department. Periodically they would review strategic decisions, again with external advice.
- The larger the fund the more likely that it will have internal investment specialists and the broader the role that they will play in investment decision making. Practice varies widely depending on a number of variables. We do show estimates of these costs in the table showing active management costs. We have not included them here as it would be likely that a large fund would certainly hold a mix of active and passive investments, and might well bring the latter function in house if it could do so at lower cost.

4.2 Active management

Some degree of active management is undertaken by the vast majority of Australian superannuation funds.

Over the past decade there has been growth in the use of multi-manager vehicles for both sector specific investment and in the construction of diversified portfolios across the risk spectrum. This is one way to reduce manager risk through diversification, and also allows for more sophisticated portfolio construction between and within asset classes.

This approach raises scale questions. A small fund is limited in the extent to which it can diversify manager risk- appoint too many managers and the size of each mandate becomes sub-scale and uneconomic.

It is partly for this reason that the Australian market has seen the rise of implemented consultants who offer “packaged” multi-manager options at both the asset class and diversified portfolio levels. This allows small to medium sized funds to access multi-manager portfolios at a far lower cost than they could themselves.

However, there is no hard and fast rule. There are many smaller superannuation funds that deliberately eschew implemented consulting products, work actively with traditional consultants and manage multi-manager portfolios to mandates, review manager performance regularly and make changes to the manager line-up as appropriate. These funds acknowledge the higher costs entailed but point to evidence that this approach is in the best interests of members.

In our analysis we have assumed that smaller funds, investing actively, would use implemented products in the way described. It produces a lower cost but this is reasonable given the philosophy underpinning MySuper and the purpose of this report.

A small fund, indeed any fund, could still create its own multi-manager portfolio if it chose but that would involve a substantially higher investment cost and it would behove the trustee to justify those higher costs in terms of value to members.

There is legitimate difference of opinion about when it becomes more efficient and practicable to bring manager selection and portfolio construction in-house. In this report we have assumed that this occurs at an asset value somewhere in excess of $2 billion, but we are not wedded to this number.

In practice, we generally observe a gradual shift towards greater trustee office investment expertise and internal responsibility for decision making as funds get larger.

In our analysis we have assumed that funds with about $5 billion or more will manage assets internally to mandate, using a combination of internal resources and external advice and research. We have followed general Australian practice which employs managers to invest and has the internal department effectively working with the trustee to set strategy and "manage the managers".

We know that this approach is under active review by some large Australian funds.

To begin with we exclude investment in alternatives.

Cost numbers

The following table show our cost estimates.

<table>
<tr><th colspan="11">Cost of investing Actively (Basis points)
Excluding alternatives</th></tr>
<tr><th rowspan="2">Asset class</th><th colspan="2">Asset allocation</th><th colspan="7">Total MySuper fund asset size $ millions</th></tr>
<tr><th>Balanced 70/30</th><th>Defensive 30/70</th><th><100</th><th>500</th><th>1,000</th><th>2,000</th><th>5,000</th><th>10,000</th><th>>20,000</th></tr>
<tr><td>Aust shares</td><td>30%</td><td>15%</td><td>50</td><td>45</td><td>40</td><td>38</td><td>35</td><td>27</td><td>22</td></tr>
<tr><td>Int'l shares</td><td>25%</td><td>15%</td><td>70</td><td>55</td><td>50</td><td>48</td><td>44</td><td>38</td><td>34</td></tr>
<tr><td>Emerging markets</td><td>5%</td><td>0%</td><td>100</td><td>90</td><td>80</td><td>78</td><td>70</td><td>66</td><td>61</td></tr>
<tr><td>Aust listed property</td><td>3%</td><td>0%</td><td>40</td><td>35</td><td>30</td><td>28</td><td>25</td><td>21</td><td>19</td></tr>
<tr><td>Aust unlisted property</td><td>3%</td><td>0%</td><td>80</td><td>70</td><td>65</td><td>63</td><td>61</td><td>58</td><td>53</td></tr>
<tr><td>Global listed property</td><td>5%</td><td>0%</td><td>80</td><td>70</td><td>65</td><td>63</td><td>55</td><td>50</td><td>45</td></tr>
<tr><td>Aust FI</td><td>15%</td><td>35%</td><td>30</td><td>25</td><td>20</td><td>17</td><td>15</td><td>12</td><td>10</td></tr>
<tr><td>Int'l FI</td><td>10%</td><td>25%</td><td>30</td><td>25</td><td>20</td><td>17</td><td>15</td><td>12</td><td>10</td></tr>
<tr><td>Cash</td><td>5%</td><td>10%</td><td>25</td><td>18</td><td>12</td><td>10</td><td>7</td><td>5</td><td>3</td></tr>
<tr><td>Internal team***</td><td></td><td></td><td rowspan="2">8</td><td rowspan="2">7</td><td rowspan="2">6</td><td rowspan="2">6</td><td>6</td><td>5</td><td>4</td></tr>
<tr><td>Custody Costs**</td><td></td><td></td><td>3</td><td>2</td><td>1</td></tr>
<tr><th colspan="11">Overall portfolio cost (Basis points)</th></tr>
<tr><td>Balanced option (70/30)*</td><td></td><td></td><td>62</td><td>53</td><td>46</td><td>44</td><td>43</td><td>36</td><td>30</td></tr>
<tr><td>Conservative option (30/70)*</td><td></td><td></td><td>47</td><td>39</td><td>33</td><td>30</td><td>31</td><td>24</td><td>20</td></tr>
</table>

* *Numbers shown should be viewed as centred within a range extending ±2-3 basis points*

** *Where the fund holds the assets via a mandate with the investment manager, otherwise close to zero*

*** *Includes cost of asset consultants and external advice generally. Numbers shown are within a range of ±1 basis points*

Comment

A review of Product Disclosure Statements reveals that the fees deducted from investment returns for a "balanced" diversified portfolio vary for a number of reasons.

These include:

- Manager costs, which can and do vary widely. Some managers command a premium. Some managers are on performance based fees that themselves can be very significant;
- The actual asset allocation of what is called a "balanced" fund might itself vary materially between funds; and
- Many funds express all or part of the administration fee charged to members as a percentage of account balance and/or deduct it from the return.

For this report we have sought to isolate all non investment related "fees" deducted from returns and assume that the remainder reflect investment related fees paid to third parties. We then add all direct (internal) investment fees recorded in P&L statements, expressing them as a % of assets.

We are confident of the costs presented for funds below $2 billion given our experience in assisting funds go to the market for implemented services. We would fully expect the implemented consultants to offer a lower (basis point) fee for even larger mandates, thereby setting a "bar" to be met by those making a positive decision to construct their own portfolios.

The use of an implemented product does reduce the need for internal involvement but it does not by any means eliminate it. The trustee and its staff still have a responsibility to ensure effective oversight and to seek independent advice. Internal costs can still be material and for small funds appear even more significant.

For funds exceeding $5 billion, we have assumed that management is undertaken internally with external advice and assistance as required. There are not that many funds of this size, and so it is difficult to present statistically reliable numbers.

The numbers we use are based on our own internal research, and seek to mitigate the impact that performance fees have had in recent times.

4.3 Active management: with alternatives

The possibility of investing in alternative asset classes adds a new dimension to the analysis of potential costs.

There are a large number of asset classes which, may be defined as "alternatives". Some have existed for many years, while some are relatively recent additions to the suite of options available to superannuation funds.

Alternatives can be complex...

There is also some controversy surrounding the nature and inherent character of some of these investments. Some are classified as "growth", others as "defensive". Yet some so-called defensive assets have been amongst those most exposed during the Global Financial Crisis.

The reality is that the nature and structure of these investments come in so many forms and guises that it often requires much greater scrutiny and research to fully understand them ahead of fully informed purchase.

... As can be estimating costs

In some alternative classes the investment by a fund is in a vehicle which itself invests in managers who deduct their fees before returns are credited to the investment vehicle. This last point highlights a potential difficulty that exists in measuring the cost of some "fund of fund" products. The only fee visible is that deducted by the direct vehicle. Downstream fees are not always quantified.

Liquidity

The other major characteristic of some alternative assets is that they can be relatively illiquid. This is compounded by the fact that some assets are unlisted and so it is necessary to have the assets periodically valued by professionals.

The result can be additional costs.

What we have assumed

To incorporate the effect of investing in alternatives it is necessary to make a number of assumptions.

1. Exposure to alternatives is something that differs markedly within different sectors of the superannuation industry and between funds. Generally, it has been the larger Industry Funds that have invested more into infrastructure and some other illiquid alternative classes, partly because they have had less need for liquidity than other more corporate based funds and partly because of their willingness to team together on major projects.

2. We have assumed that the exposure to alternatives will be limited to 10% of assets in each of the already described Balanced and Conservative portfolios. In effect 10% of those portfolios will be diverted to a bundle of alternative assets.

    i. The 10% alternatives in the Balanced portfolio will be split 70/30 between those alternative asset classes classified below as Growth or Defensive respectively. We call this the “Balanced Bundle”;

    ii. The 10% alternatives in the Conservative portfolio will be split 30/70 between those alternative asset classes classified below as Growth or Defensive respectively. We call this the “Conservative Bundle”;

    iii. The classification of alternatives into Growth and Defensive is somewhat arbitrary. Most do not fit naturally into this somewhat anachronistic (but still widely used) classification. It does not have any significant impact on the conclusions presented in this report.

Alternative “asset classes”	
Growth	**Defensive**
Private equity	Global credit
Global macro	Leveraged loans
Event - driven	Global high yield
Market neutral	Global listed infrastructure
Long short	Global unlisted infrastructure
Commodities	Infrastructure debt
	RMBS
	Hedge funds
	Fund of hedge funds (excluded)

3. Costs have been estimated from data we have seen in respect of some, generally larger, funds. However, it is difficult to translate this data into firm and precise estimates of the cost of alternatives. The numbers range widely and moreover, the nature of the assets involved often entails significant management costs, as well as increased time and effort from the investment wing of the trustee office.

4. Should we assume that smaller funds invest in alternatives? There is no doubt that some product manufacturers are seeking to satisfy the demand for such assets within smaller funds by offering “alternative” portfolios. Implemented consultants are introducing some exposure to alternatives.

But there are issues surrounding liquidity, and so we have not produced a cost number for alternatives for a fund below $100 million. For all larger funds we have used the same 10% exposure to the Balanced and Conservative alternative bundles;

5. Our work does bring us into contact with funds of all shapes and sizes. We generally observe lower allocations to alternatives in smaller funds and many restrict themselves to investment in only some of the alternative asset classes. This suggests that we could model exposure to alternatives and the respective Growth and Defensive bundles of alternatives by fund size. This adds another layer of complication to the analysis and acts to understate the scale benefits enjoyed by larger funds. After all, if these investments add value to members then funds should act accordingly. We have, therefore, adopted the same bundle and allocations for all fund sizes;

6. It is not always possible to invest passively in alternative asset classes. We have, therefore, restricted our analysis of alternatives to an extension of active management.

Cost numbers

This shows our estimate of costs where a portion of assets are invested in alternatives.

Cost of investing Actively (Basis points) Including alternatives	Total MySuper fund asset size $ millions					
	<500	1,000	2,000	5,000	10,000	>20,000
Overall portfolio cost (Basis points) Excluding Alternatives (see earlier table)						
Balanced option (70/30)*	53	46	44	43	36	30
Conservative option (30/70)*	39	33	30	31	24	20
Cost of alternative assets bundles						
Balanced Bundle**	182	151	140	109	101	89
Conservative Bundle**	153	125	116	89	77	67
Overall portfolio cost (Basis points) Including Alternatives (exposure 10% of total)						
Balanced option (70/30)***	65	57	54	50	43	36
Conservative option (30/70)***	50	42	39	36	30	24

* *Numbers shown should be viewed as centred within a range extending ±2-3 basis points*

** *Numbers shown should be viewed as centred within a range extending ±15 to 20 basis points*

*** *Numbers shown should be viewed as centred within a range extending ±3-5 basis points*

Comments

The table demonstrates the well known fact that investment in alternatives involves significantly higher fees than those generally paid in the more traditional asset classes. Nevertheless, our estimates suggest that some alternative exposure should be achievable at quite reasonable investment costs, even for relatively small superannuation funds.

Our calculations are based on 10% of assets being invested in alternative assets. The effect has been to increase overall portfolio costs by between:

- 5 and 13 basis points for the Balanced portfolios;
- 5 and 12 basis points for Conservative portfolios.

Scale is again the dominant factor, with the increase being:

- In excess of 10 basis points for the smaller funds; and
- In the order of 5 basis points for very large funds.

Alternatives classified as Growth tend to cost more than those classified as Defensive and it is also our experience that performance based fees can be significant and complex.

It is a separate question and one outside the scope of this report, whether such an exposure is appropriate given the specific factors that might be present within a given superannuation fund. We especially have in mind the need for liquidity.

We know that the technical justification for many alternatives is diversification and various protections against downward market movement. Our table shows that in some cases this does not come cheaply.

4.4 Investment costs in summary

We can draw together our estimate of the costs presented above into a single table.

	Total investment costs (Basis points) Total MySuper fund asset size $ millions						
	<100	500	1,000	2,000	5,000	10,000	>20,000
Passive investment							
Balanced portfolio	31	21	16	10	7	4	2
Conservative portfolio	24	14	12	8	5	3	2
Active investment (excluding alternatives)							
Balanced portfolio	62	53	46	44	43	36	30
Conservative portfolio	47	39	33	30	31	24	20
Active investment (including alternatives)							
Balanced portfolio	---	65	57	54	50	43	36
Conservative portfolio	---	50	42	39	36	30	24

5 Operating costs

Operating a superannuation fund is a complex matter requiring a host of skills and infrastructure. It is rare for a fund to possess all of that which is necessary internally. Funds rely on partners to varying degrees.

The major exception to this is the major wealth management institutions that have built extensive in-house proprietary administration systems and have access to capital to invest in that infrastructure.

A difficulty is that the definition of administration and the services that it entails is itself evolving. The graphic below is based on internal work that we have done and seeks to show the range of functions and services and the potential breadth of partnering arrangements. It includes some elements of service related to investment

		Scale economies demanded				Service quality the critical issue
The Customer Interface	Call Centre	Completely outsourced, shared with other clients	Completely outsourced, dedicated staff for fund	Completely outsourced, fund hand-picks staff	In-house staffing (systems could still be outsourced)	
	Website	Generic shell website, may have customised logo and colours	Design sourced internally, content supplied externally		Design and content sourced internally (may still use third party builder and host)	
	Mail room	All mail sent to third-party office for processing	Mail processed (including scanning) by local bureau and forwarded to third party administrator		Mail processed (and scanned) internally	
Back-office processing	▪ New members, ▪ Benefit payments ▪ Contribution upload ▪ Annual review ▪ Investment transactions ▪ Compliance and reporting	Completely outsourced, shared with other clients	Completely outsourced, dedicated staff for fund	Completely outsourced, fund hand-picks staff	In-house staffing (systems could still be outsourced) Outsourced staff, located in fund's own office	
Record-keeping systems	Member records	System run and used by administrator (system may be supplied and maintained by a third-party)		Commercially-supplied system run in-house on own hardware	System developed, maintained and run in-house on own hardware	
	Transactions	Managed by third-party administrator as part of overall administration service			Separate general ledger package or integrated with member-record-keeping system (rare)	
	Investments			Normally handled by an external Custodian		

Where a fund sits and the policies it adopts depend in no small part on the overall business and competitive strategies.

5.1 Current industry practices

While industry practice varies widely we can draw some conclusions:

- Most corporate funds will partner with a third party to deliver the bulk of administrative services. The trustee office will typically consist of a secretary and support staff, which may or may not be full time, and where a major part of their role is to liaise and manage service providers;
- Industry Funds generally work with an administrator who undertakes day to day processing where scale benefits are most important, especially amongst the larger funds. Practice is much more variable amongst smaller funds where a number operate their own administration departments often using purchased software packages or using boutique administration service companies. It should be pointed out that a number of industry funds have taken equity positions in their administrator. In either event, a trustee office is maintained;

- Wealth management organisations generally maintain their own internal administration capability using purchased or purpose built administration software. An independent trustee office is maintained and this works closely with the administration arm;
- Public sector funds sometimes use a specialist administrator that evolved with the fund itself. In some cases these divisions have corporatized, and are now promoting themselves as third party administrators to the industry as a whole;
- There are of course exceptions to all of the above.

Specialist administration companies

There has been significant rationalisation amongst administrators over the past few years, as growing industry complexity and the importance of scale in delivering competitive outcomes and in justifying investment have become more important.

There are now, at most, only a handful (or so) of firms that have the depth and resources to be able to deliver competitive services to the mass superannuation market. There are a number of other firms that act as administrators to a relatively small client base but these firms rarely capture new business.

In part this reflects pricing which in the past has been insufficient to attract new entrants. The widely held view is that “administration is a low margin business” and that the bulk of revenue and profit from superannuation comes via asset management.

There is some element of truth to this but it is also fair to say that the inefficiencies in the superannuation system, many of which are described in the SuperStream paper, have made it more difficult for administrators, particularly the mass administrators, to achieve productivity gains and make the most of electronic processing in all its forms.

We have, therefore, seen the emergence of three distinct types of administration platforms over the past few years:

- High touch administrators who, notwithstanding aged systems, have developed the ability to electronically engage with members and through the use of web based and other functionality transferred much of the day to day transactions to what is effectively a user pays environment – in the same way as the banks have utilised ATMs. They have been able to contain costs somewhat and at the same time, have developed value add services for funds that want to engage more closely with their members. They generally resist all paper based transactions;
- The large mass administrators who possess scale and the benefits of incumbency. They too have some developed capability to move to a user pays transactional system but are hostage to the manual, paper based, member interactions that are all too common in this country. This also restricts their ability to reduce costs, contributes to significant amounts of rework, and has limited their ability to develop leading edge value add services to assist funds better engage with members;
- A number of small administrators who have just one or two small to medium size clients.

There is also:

- A latent administrative capability of high standard within the major wealth management organisations, which is essentially quarantined to the clients of those organisations. This is geared towards high touch. It is not usually sold as a standalone service; and
- A number of in-house administration functions maintained by individual funds.

5.2 Components of operating costs

It is therefore apparent that total operating costs are a combination of:

Third party administrator fees

Fees paid to external administrators which will include a profit margin. We acknowledge the view that administration margins are thought to be low. However, it is not within scope for us to consider or comment on an appropriate margin for the future. Should margins increase then this would clearly flow through to increased costs.

Internal costs

Internal or trustee office costs can include some costs that have traditionally been packaged under the administration heading, especially services central to member engagement. However, trustee office costs also include, to the extent not outsourced:

1. Trustee fees & support, including reporting
2. Staff salaries and associated on costs
3. Compliance, audit and statutory fees
4. Management of service providers
5. Insurance claims management
6. Internal IT and accommodation
7. Other corporate overhead
8. Postage, handling
9. Marketing and business development

Some funds have brought some of the functions typically provided by third party administrators in-house and for these funds we will see internal costs rise and third party fees reduce. A number of funds do virtually all administration in-house, have a relatively large number of employees and almost all operating costs appear on the funds P&L statement.

Intra-fund advice

Funds have been providing assistance to members for some time in a number of different ways and financing that assistance in ways ranging from user pays at one end to a general charge for all members at the other.

Calculators and useful information are now routinely provided on websites. Service centres increasingly include (at least some) people qualified to provide assistance beyond simple statements of fact.

A number of funds have gone further and (often with external assistance) are now enabled to deliver advice. We sometimes see simple and limited advice delivered at no extra cost to the member, which means that the cost is included in standard fees.

Many others are now considering how to respond to the ASIC RG 200, which is proposed to be a compulsory feature of MySuper.

At this point, we reiterate the central role that core administration plays in delivering intra-fund advice. Those funds delivering advice must have access to accurate and up to date information about the member and their current interest in the fund. They require what the industry terms a “single member view”, where all member information is quickly and inexpensively available for use.

While this sounds simple, even rudimentary, it has proven to be a major and costly challenge for systems designed at a time when batch processing was the norm and where the only regular contact envisaged with a member was the annual mail out of statutory material.

Systems have, or are, in the process of being upgraded, as is the ability to reduce transactional costs through the use of electronic channels, and straight through processing. These capabilities are already in the DNA of the better administration systems, which are generally found amongst the corporate master trusts and the wealth management organisations.

Those not able to easily upgrade will need to seek external assistance, or contemplate more fundamental change, it in order to offer intra-fund advice at a reasonable cost.

Bells & whistles

The MySuper paper makes it clear that members of MySuper funds should not be made to pay for “bells and whistles” that they will not make use of and that their cost should be quarantined to “Choice” members.

We repeat here that in this report we have extracted all costs associated with full comprehensive advice and distribution as provided for in MySuper. Consequently, the points made in the next few paragraphs refer to whatever “bells and whistles” are associated with operational functionality, flexibility and the ability to engage with individual members to assist them.

We think it will be difficult to extract these costs as they are effectively built into the fund’s core operating infrastructure.

It makes little sense and would be uneconomic for a fund to maintain separate operating infrastructures for their MySuper and Choice products. We are firmly of the view that funds will have a single system.

We believe that in many cases it will be difficult for trustees and their providers to accurately account for the cost of that portion of infrastructure that is solely attributable to “bells and whistles” and suspect that it would only constitute a relatively minor part of the total cost. However, if that cost was quarantined then a relatively minor saving for the MySuper members could translate into a substantial increase in costs for Choice members.

A simple example can be used to illustrate this:

Suppose a fund is currently charging all operating costs at a fixed $100 per member per annum:

- MySuper members comprise 80% of members; and
- 10% of total operating costs are attributable to “bells and whistles”;

If we quarantine the cost of the “bells and whistles” to Choice members but assume that total fund costs do not reduce then:

- Costs charged to the 80% MySuper members will reduce by 10% to $90 per member; but
- Costs charged to the 20% Choice members will increase to $140 in order to make good the shortfall.

In fact, total costs might actually increase marginally, as funds incur the cost of allocating costs in whatever way is prescribed.

The figures are even more dramatic where the proportion of MySuper members is greater. If they are 90% of total members then the charge for Choice members would increase by 90% to $190.

Of course if the cost of bells and whistles is much lower, then the impact as well as the case for change is weakened.

5.3 Operating cost excluding intra-fund advice

We have a significant amount of data that we can use to provide estimates of costs excluding intra-fund advice, including our own research, results of tenders and other client work.

As already mentioned we believe that little intra-fund advice costs are included in the data that we have used and our research has excluded advice and distribution - though we know some marketing and sales costs are included.

Current operating infrastructure will underpin MySuper

Current fund systems, people and processes will form the basis of any MySuper product established by the sponsors of a current fund.

We are consequently comfortable that the costs presented below will be representative of the costs that could be experienced by MySuper products of varying sizes. These costs will, to varying degrees, include a "bells and whistles" component but we do not believe it is very significant and we see some difficulty in separating it out in practice.

Cost numbers

The following table shows operating costs (excluding intra-fund advice) for funds of varying sizes. All costs are expressed as annual amounts per member.

Estimated operating costs excluding intra-fund advice
for MySuper products of varying sizes
(as $ per member per annum)

Fund size: $millions	<100	500	1,000	2,000	5,000	10,000	>20,000
Fund size: membership*	4,000	20,000	40,000	80,000	200,000	400,000	800,000
Third party administration fees**	$124	$90	$78	$68	$57	$49	$43
Trustee office**	$120	$105	$71	$46	$31	$28	$23
Total operating costs (excl. advice)* **	**$244**	**$195**	**$149**	**$114**	**$88**	**$77**	**$66**

* *Assuming as instructed an average account balance of $25,000*

** *Actual third party admin fees will depend on the range of services contracted for. As already explained, this will possibly differ widely from fund to fund. In the extreme, if all administration is undertaken in-house it will be zero. But we will see a corresponding increase in internal (i.e. Trustee office costs). Because of the above, we can be more confident in estimating total costs. Our estimates are based on research that predates ASIC RG 200 and so, while we know there were some funds that were providing advice, the costs would be minor. We can, therefore, confidently add to this our estimate of the cost of intra-fund advice*

*** *Numbers should be taken as being centred on a range extending ± $5-$10*

Comment

These are significant variations in operating costs from fund to fund. The costs shown are representative of "averages" at the various fund sizes.

The table shows strong scale economies.

It is important to highlight that it is possible for smaller funds to access some of the benefits of scale by partnering with service providers who themselves have scale. This is true of many services, including administration. Yet, an administrator does incur quite high set up costs in putting a system in place for a new client and these are amortised over a number of years (typically 3 to 5). For a small fund this translates into a significant extra cost per member.

On top of this we know that some funds, including some that are quite small, have appointed third party administrators who themselves lack scale or have chosen to self administer.

The result is demonstrated in the table which shows small fund costs are much higher.

The evidence is clear. Larger funds are able, other things equal, to provide basic operational services at a lower per member cost.

5.4 Cost of intra-fund advice

Total intra-fund advice depends on two basic factors: the cost of delivering the service to each individual member and the likely demand for the service.

We refer to Section 3.3 where we presented a view that quality administration platforms were reaching the point where much of the advice was capable of being covered as part of ordinary business, through electronic and telephone contact.

This capability is largely recognised within current operating costs.

The major additional cost will be related to assistance on specific and more complex limited personal advice.

We are able to make some informed estimates of the cost of delivering general and limited advice to individual members from some of the work we have undertaken over recent months. A number of third party providers specialise in these services and provide some insights into fees.

Nevertheless, data is limited and we have had to make some assumptions on the extent to which unit costs would reduce with demand.

Having said this we should point out that opinions do vary and in discussions within the industry we have had opinions expressed that the individual cost of advice could be twice the estimates used in this report.

But, as will be seen, the total cost is incremental within total fund costs.

Member demand for this service is difficult to quantify. We do not hold strongly to the levels assumed in this report, though in discussion with funds they are not felt to be unreasonable.

Cost numbers

Estimated costs of intra-fund advice for MySuper products of varying sizes (as $ per member per annum)

Fund size: $millions	<100	500	1,000	2,000	5,000	10,000	>20,000
Fund size: membership	4,000	20,000	40,000	80,000	200,000	400,000	800,000
Demand for advice (% of total membership)							
General advice	10%	10%	10%	10%	10%	10%	10%
Personal advice	5%	5%	5%	5%	5%	5%	5%
Cost of individual piece of advice $							
Cost general	75	60	50	45	40	35	30
Cost personal	200	170	150	130	120	110	100
Total cost for total fund $pa	**$70,000**	**$290,000**	**$500,000**	**$880,000**	**$2,000,000**	**$3,600,000**	**$6,400,000**
Total cost $ per member per annum	**$18**	**$15**	**$13**	**$11**	**$10**	**$9**	**$8**
Total cost $ per member per week	**$0.34**	**$0.28**	**$0.24**	**$0.21**	**$0.19**	**$0.17**	**$0.15**

Comment

Calculated costs for advice are only a fraction of total operating costs and represent a relatively small charge for each (and every) member. To reinforce the point, we have in this table also calculated the effective weekly charge. This does not alter the cost, but is consistent with industry practice.

We have not included any cost for comprehensive advice in these calculations. Rather, we have assumed that if this was offered by a fund then it would be financed on a user pays basis. Those fees would be disclosed in advance of a member "purchasing" this additional service and under the MySuper proposals could be met out of the member's account balance.

5.5 Total operating costs

We can now draw all estimated operating costs together into a single table

Cost numbers

Estimated operating costs for MySuper products of varying sizes
(as $ per member per annum)

Fund size: $millions	<100	500	1,000	2,000	5,000	10,000	>20,000
Fund size: membership*	4,000	20,000	40,000	80,000	200,000	400,000	800,000
Third party administration fees**	$124	$90	$78	$68	$57	$49	$43
Trustee office**	$120	$105	$71	$46	$31	$28	$23
Total operating costs (excl. advice)* **	**$244**	**$195**	**$149**	**$114**	**$88**	**$77**	**$66**
Intra-fund advice****	$18	$15	$13	$11	$10	$9	$8
Total operating costs (incl. advice)	**$262**	**$210**	**$162**	**$125**	**$98**	**$86**	**$74**

* *Assuming an average account balance of $25,000*

** *Actual third party admin fees will depend on the range of services contracted for. As already explained, this will possibly differ widely from fund to fund. In the extreme, if all administration is undertaken in-house it will be zero. But we will see a corresponding increase in internal (i.e. Trustee office costs)*

*** *Because of the above, we can be more confident in estimating total costs. Our estimates are based on research that predates ASIC RG 200 and so, while we know there were some funds that were providing advice, the costs would be minor. We can therefore confidently add to this our estimate of the cost of intra-fund advice.*

**** *Based on the costs and volumes already described.*

Comment

One thing is clear: there are large scale economies in operating costs. It could be argued that there should be less scale effects in the delivery of advice than we have assumed and we acknowledge that might be true. But this does not materially change our conclusion because intra-fund advice is only a relatively small component of total operating costs.

Moreover, there are some funds where current operating costs (excluding bundled advice, platform fees and the like) are substantially higher than suggested in the table.

We are firmly of the view that the best way to describe fund costs is as an amount deducted annually from accounts, as they are logically related to fund membership.

5.6 Total operating costs: varying size of account balance

From an individual member's perspective, a charge of, say, $250 per annum consumes a far greater proportion of a $10,000 account than it would a $200,000 account.

In the next table we re-express the total annual per member operating cost as a % of the member's account for a range of possible account balances.

Estimated total operating costs for MySuper products of varying sizes
(basis points for varying account sizes)
&
Inclusive of cost of intra-fund advice

Fund size: $millions	<100	500	1,000	2,000	5,000	10,000	>20,000
Fund size: membership*	4,000	20,000	40,000	80,000	200,000	400,000	800,000
Account size							
$10,000	262	210	162	125	98	86	74
$25,000	105	84	65	50	39	34	30
$50,000	52	42	32	25	20	17	15
$100,000	26	21	16	13	10	9	7
$250,000	10	8	6	5	4	3	3

* *Membership based on an average account balance of $25,000*

These estimates follow industry practice which has tended to only look at fees in terms of "MER". They show that a member with a $10,000 account in a $100 million dollar fund will likely find administration costs of the order of 2.62% per annum. Of course, in the same fund there might be a member with a $250,000 account. The $262 is only 10 basis points (0.10%) and looks, when expressed this way, very small.

All of these costs are before any investment related costs are deducted from returns, and exclude any bundled advice fees.

They serve to illustrate the inefficiency that results from any Australian having multiple "lost", and generally quite small, accounts steadily eroded by regular deduction of administration and other costs.

5.7 Operational reserves

We close this section with an observation about the superannuation industry's approach to establishing and maintaining operating and contingency reserves.

There is no standard. Some funds do maintain reserves but to varying amounts. Some funds rely on service provider contracts in whole or in part to meet costs of errors or rely on insurance arrangements to meet claims. Strictly, all funds should have clear and well thought through policies as part of their risk management plans.

We cannot be confident that this is being done in a way that renders the numbers presented in this report as being fully inclusive of adequate provisioning.

6 Total MySuper costs

We are now in a position to bring investment and operating costs together to estimate the total costs that could be expected under the MySuper proposals presented to us in the Paper.

It is clear that there will be no single answer. There are a number of factors that will influence total cost including:

- Scale, both in terms of assets and membership;
- Investment approach: active or passive
- Asset allocation; and
- Use of higher cost alternative asset classes.

The following table shows total costs as they might vary with changes in each of these variables. For convenience we have expressed all costs as a % of assets because users will compare these numbers with industry data that is almost always presented in that form.

Estimated total costs for MySuper products of varying sizes
(all costs expressed as basis points)
Investment costs + Operating costs (incl. intra-fund advice)

Fund size: $millions	<100	500	1,000	2,000	5,000	10,000	>20,000
Passive investment							
Balanced portfolio	136	104	80	60	46	38	32
Conservative portfolio	129	98	76	58	45	37	32
Active investment (excluding alternatives)							
Balanced portfolio	166	136	111	94	83	70	60
Conservative portfolio	151	123	97	80	70	59	49
Active investment (including alternatives)							
Balanced portfolio		149	121	104	89	77	66
Conservative portfolio		134	107	89	76	64	54

7 Reliances and Limitations

We have relied on the accuracy and completeness of all data and other information (qualitative, quantitative, written and oral) provided to us for the purpose of this report. We have not independently verified or audited the data but we have reviewed it for general reasonableness and consistency. It should be noted that if any data or other information is inaccurate or incomplete, our advice may need to be revised.

This report has been prepared for the sole use of the Super System Review for the purpose set out in this report.

Yours sincerely

Wayne Walker
Deloitte Actuaries & Consultants

Michael Monaghan
Deloitte Actuaries & Consultants

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APPENDIX E: SECRETARIAT

The secretariat was established in Melbourne to assist the Panel with staff drawn from Treasury, the private sector and the regulatory agencies with responsibility for superannuation.

Secretariat:

Roger Brake and the staff of the Superannuation Unit of Treasury

Roger Brown on secondment from APRA

Pedro Café on secondment from the ATO

Scott Donald, University of New South Wales

Peggy Haines, Freehills

Hilda Miller on secondment from ASIC

Paul Murphy, UniSuper *(Consultant)*

Philip Russell on secondment from ASIC

Wilson Sy on secondment from APRA

Brad Tallents on secondment from KPMG

Sophie Trumble on secondment from ASIC

APPENDIX F: ABBREVIATIONS AND ACRONYMS

ABA	Australian Bankers' Association
AASB	Australian Accounting Standards Board
ABS	Australian Bureau of Statistics
ACR	Auditor Contravention Report
ACSI	Australian Council of Super Investors
ACTU	Australian Council of Trade Unions
ADF	Approved Deposit Fund
ADI	Approved Deposit-taking Institution
AFSL	Australian Financial Services Licence
AFTS	Australia's Future Tax System
AGA	Australian Government Actuary
AGM	Annual General Meeting
AIG	Australian Industry Group
AIST	Australian Institute of Superannuation Trustees
ALLS	Adult Literacy and Life Skills Survey
AML/CTF Act	*Anti-Money Laundering and Counter Terrorism Financing Act 2006*
APRA	Australian Prudential Regulation Authority
ASFA	Association of Superannuation Funds of Australia
ASIC	Australian Securities and Investments Commission
ASX	Australian Securities Exchange
ATO	Australian Taxation Office
AUASB	Australian Auditing and Assurance Standards Board
AUSTRAC	Australian Transaction Reports and Analysis Centre
Bps	Basis Points — a basis point is one-hundredth of a percentage point
CAMAC	Corporations and Markets Advisory Committee
CGT	Capital Gains Tax
CHESS	Clearing House Electronic Subregister System
Complaints Act	*Superannuation (Resolution of Complaints) Act 1993*
Corporations Act	*Corporations Act 2001*
Corporations Regulations	Corporations Regulations 2001
CPA	CPA Australia
CPI	Consumer Price Index

DB	Defined Benefit
DC	Defined Contribution
EFT	Electronic Funds Transfer
EPSSS	Exempt Public Sector Superannuation Scheme
ERF	Eligible Rollover Fund
ERISA	Employee Retirement Income Security Act (US)
ESG	Environmental, social and governance
FaHCSIA	Department of Families, Housing, Community Services and Indigenous Affairs
FOS	Financial Ombudsman Service
FPA	Financial Planning Association
FS(COD)	*Financial Sector (Collection of Data) Act 2001*
FSG	Financial Services Guide
FTSE	Financial Times/London Stock Exchange Group
GDP	Gross Domestic Product
GEERS	General Employee Entitlement and Redundancy Scheme
GFC	Global Financial Crisis
HILDA	Household, Income and Labour Dynamics in Australia
ICAA	Institute of Chartered Accountants in Australia
ICR	Indirect Cost Ratio
IFF	Industry Funds Forum
IFSA	Investment & Financial Services Association (to be renamed the 'Financial Services Council' with effect from 20 July 2010)
IGR	Intergenerational Report
IGT	Inspector-General of Taxation
IHA	In-house Asset
ISN	Industry Super Network
MER	Management Expense Ratio
MOU	Memorandum of Understanding
NIA	National Institute of Accountants
NICRI	National Information Centre on Retirement Investments
OECD	Organisation for Economic Cooperation and Development
PDS	Product Disclosure Statement
PSB	Payment Systems Board
PST	Pooled Superannuation Trust

RBA	Reserve Bank of Australia
REST	Retail Employees Superannuation Trust
RMP	Risk Management Plan
RMS	Risk Management Strategy
RSA	Retirement Savings Account
RSE	Registrable Superannuation Entity
SAF	Small APRA Fund
SBR	Standard Business Reporting
SCT	Superannuation Complaints Tribunal
SEC	Securities and Exchange Commission
SG	Superannuation Guarantee
SG Act	*Superannuation Guarantee (Administration) Act 1992*
SGC	Superannuation Guarantee Charge
SIS Act	*Superannuation Industry (Supervision) Act 1993*
SIS Regulations	Superannuation Industry (Supervision) Regulations 1994
SLWG	Squam Lake Working Group
SMSF	Self-Managed Super Fund
SPAA	SMSF Professionals' Association of Australia Limited
SPIN	Superannuation Product Identification Number
STP	Straight-Through Processing
SWG	Superannuation Working Group
SwimEC	Superannuation, Wealth And Investment Management Electronic Commerce
TAER	Total Annual Expense Ratio
TFN	Tax File Number
TPB	Tax Practitioners Board
TPD	Total and Permanent Disability
UK	United Kingdom
US	United States

APPENDIX G: GLOSSARY

Term	Definition
Account-based product	A product where the value of the amount from which an income stream is drawn is determined by the member's account balance.
Accumulation fund	A superannuation fund where the value of the final retirement benefit payable to members is the member's account balance at the relevant time.
Accumulation phase	The period of time over which a fund member builds the value of their benefits before retirement.
Administrator	A party contracted by the trustee to provide services such as record-keeping and member account management for the fund.
AFTS Review	The 2009 report and recommendations of the Review of Australian Future Tax System, also known as the Henry Review.
After-tax return	The return on an investment after all applicable government charges, duties and taxes have been deducted or accounted for.
Annuity	Generally, a stream of payments made at regular intervals. In superannuation, a fund member can use all or part of their benefits to purchase an annuity from an insurer in order to receive the value of their benefit as an income stream.
APRA-regulated fund	All superannuation funds regulated by APRA under the SIS Act, but does not include SMSFs.
Asset-based fees	A fee payable for a service calculated by reference to the value of the assets to which the service relates.
Asset allocation	The distribution of a superannuation fund's assets in investments in different classes of assets, such as equities, fixed interest, cash and real property.
Auto-consolidation	A process by which different superannuation accounts in respect of the same person are automatically consolidated within a superannuation fund and across different funds.
Bundling	Building in a number of services or features in a single product which cannot be separated.
Choice architecture	A model for the regulation and governance of the superannuation system where regulation and trustee responsibility is based on the degree to which members make choices and take responsibility for their super.
Choice product	A superannuation product in the choice architecture model (described in chapter 1) where a member has made a choice that their superannuation would not be in MySuper or their own SMSF.
Clearing house	A service provided to employers effectively outsourcing the distribution of superannuation contributions and information to superannuation funds. The clearing house receives a single payment from the employer and then distributes all the necessary contributions on behalf of the employer to the funds chosen by the employees.
Commission	A fee payable as an incentive or reward to the seller of a product, usually based on the value of the goods or services sold.
Consolidation (of accounts)	The transfer of one or more of a person's superannuation fund accounts into a single or a reduced number of superannuation accounts, with resulting administration fee savings.
Consolidation (of industry)	The gradual process whereby the number of superannuation funds is reduced as a result of fund mergers.

Term	Definition
Cost cross-subsidisation	Where members of one fund, or one investment option, subsidise costs attributable to others.
Custodian	An entity that acts as a bare trustee and holds assets of a superannuation fund on behalf of the superannuation fund trustee. The custodian holds the legal title to the asset and acts only at the direction of the fund trustee.
Default fund	The superannuation fund to which an employer's Superannuation Guarantee contributions will be paid if the employee does not direct the employer to make the contributions to a fund chosen by the employee.
Default investment option	The investment strategy the trustee of a superannuation fund will use when investing the assets of the fund unless a member directs the trustee to invest their benefits (wholly or partly) in another strategy made available by the trustee for selection by members.
Default level of cover	The member's level of insurance cover in a superannuation fund that will apply unless the member opts-out of cover or is able to obtain a higher level.
Deferred annuity	An annuity where payments do not commence immediately. In superannuation, the commencement of payments is tied to the circumstances in which a superannuation fund could pay benefits.
Defined benefit	A superannuation benefit the value of which is determined by reference to a formula.
Defined benefit fund (or plan)	A superannuation fund where contributions are pooled and are not allocated to particular members. Under the SIS Act, if a fund has even one member with a defined benefit, it is treated as a defined benefit fund.
Defined contribution fund	An alternative expression for accumulation fund.
Drawdown phase	Another expression for post-retirement.
E-commerce	The linked electronic transmission of data and money.
Economies of scale	The effect of generally lowering the cost of each iteration of an activity when the activity is conducted on an increasing scale. In relation to a superannuation fund, scale advantages can relate to investment fees, in-house investment expertise, private placement capabilities, ability to spread investment risk through diversification, reduced administrative unit costs, and enhanced availability of education, information and service. Another example is using the pool of members in a fund to purchase insurance on a group risk basis, rather than individually.
Eligible rollover funds (ERFs)	Superannuation funds or approved deposit funds that are eligible to receive benefits automatically rolled-over from other funds. ERFs typically accept superannuation money from other funds where the member has become 'lost'.
Exempt public sector superannuation schemes (EPSSS)	Funds that provide benefits for government employees, or are schemes established by a Commonwealth, State or Territory law that are not directly subject to the SIS Act and APRA regulation.
First non-associated level	In relation to the investments made by a superannuation fund, the first investment in a layered structure of investments that is not associated with or related to the trustee of the fund.
Flipping	The practice of a member being automatically moved from one division of a superannuation fund to another (generally to a 'personal' division or plan) on cessation by the member of the particular employment to which the original fund division related.
Forecasts of retirement benefits	Advice from the trustee of a superannuation fund to fund members that aims to provide an indication of the value of their ultimate retirement benefit.

Term	Definition
GEERS	General Employee Entitlement and Redundancy Scheme — a Government scheme to compensate employees who lose their jobs as a result of the liquidation or bankruptcy of their employer and who are owed a range of employee entitlements.
Grandfathering	The preservation and continuation of a state of affairs created by legislation, usually beneficial, when new and less advantageous legislation is introduced.
Group risk insurance	Insurance acquired by a superannuation fund trustee that collectively covers all the persons who may, from time to time, be members of the fund and which covers fund members in the event of death, TPD and loss of income due to ill-health.
Henry Review	Another name for the AFTS.
Inactive account	Generally, a member account in a superannuation fund where the fund has not received a contribution or rollover in respect of the member within the last five years.
Income protection insurance	Insurance acquired by the trustee of a superannuation fund in respect of a fund member, the proceeds of which are used by the fund trustee to provide periodic benefits to continue (wholly or partly) the income that the member was receiving before commencing a period of ill-health or temporary disability.
Instalment warrant	A form of derivative or financial product that entails borrowing to invest in an asset, such as a share or real property (the underlying asset), with limited risk to the investor. In its simplest form, the investor makes an upfront payment, which typically includes prepaid interest and borrowing fees. The underlying asset is held in trust during the life of the loan to provide limited security for the lender. The investor is required to pay one or more future instalments to the lender.
Intra-fund advice	Current ASIC arrangements under which superannuation fund trustees that hold an AFSL to provide personal financial product advice can give advice to fund members about certain aspects of their existing interest in the fund, with the level of inquiry and consideration in relation to that advice set by the trustee's fiduciary duty to members, rather than the Corporations Act. Also includes ASIC guidance in relation to giving personal advice to fund members only in relation to specific fund features under the generic standards in the Corporations Act. The regime is due to be expanded by the Government under its Future of Financial Advice package and the final report generally uses the expression in that expanded sense.
Investment option	An investment strategy formulated by a superannuation fund trustee in which a fund member may select to have all or part of their benefits invested.
Investment risk	The uncertainty with respect to the financial return an investment will generate. In an accumulation fund, the investment risk in relation to the fund's assets affects the value of the investment return credited, or debited to, members' accounts.
Issues Paper	One of the Panel's publications seeking submissions in relation to each phase of the Review: Phase one — Governance, 25 August 2009; Phase two -Operation and Efficiency, 16 October 2009; and Phase three — Structure (Including SMSFs), 14 December 2009.
Large APRA fund	An APRA-regulated fund with more than four members, including ERFs, but excluding PSTs.

Term	Definition
Legacy product	Generally, an older-generation superannuation product held by fund members that is no longer available for issue to new members.
Lifetime annuity	An annuity payable over the life of the recipient.
Liquidity	The capacity of a superannuation fund trustee to transform fund assets quickly into cash without a material change in price to make timely payments as required, such as pension payments or requests from members to transfer their benefit to another fund.
Longevity risk	The uncertainty about how long a particular person (or group of people) will live. For a superannuation fund member, it is the risk an income stream superannuation benefit will be depleted before they die. For providers of lifetime annuities, it is the risk recipients will live longer, and draw more benefits, than the provider has allowed for.
Lost member	Generally, a member of a superannuation fund determined by the trustee, in accordance with the SIS Regulations, as uncontactable or in relation to whom no contributions have been received by the fund in the last five years.
Lump sum	An amount of a superannuation benefit paid to a fund member as a stand-alone cash amount. Benefits can be paid as one or more lump sums.
Member	A person who holds an interest in a superannuation fund either because they are accruing benefits to provide income in retirement or because they are receiving benefits from the fund.
Member protection	Regulatory arrangements under which, generally, superannuation fund members with an account balance of less than $1,000 cannot have that balance debited for fund administration costs greater than the earnings on the account.
MySuper product	A superannuation product in the choice architecture model where, among other things, members rely on the trustee to make decisions for them with respect to investment and insurance.
Net investment return	The return on an investment after deducting all costs relating to the investment, such as fees, brokerage, administration and taxation.
Operational risk reserve	Part of the asset base of a superannuation fund aggregated and held for the specific purpose of providing financial resources to allow the trustee to mitigate operational risks, such as unit pricing errors, where costs are not met by third parties.
Outsourcing	Where a superannuation fund trustee contracts for another person to perform activities in relation to the fund, such as fund administration and investment management, on behalf of the trustee.
Panel	Collectively, the chair and the part-time members appointed by the Government to conduct the Review.
Performance-based fee	A fee payable calculated by reference to the performance of an investment made by a superannuation fund trustee or to the performance of a superannuation fund or investment option.
Phase (of the Review)	A phase to which the Review's Issues Papers related — Phase one — Governance; Phase two — Operation and efficiency; and Phase three — Structure (including SMSFs).
Portability	A fund trustee's obligation under the SIS Act to pay (within a 30-day period) the value of a member's benefits to another superannuation fund on request of the member.
Post-retirement	The phase of a person's life during which the person has retired from the workforce, has usually ceased to build superannuation benefits and begun to rely on their benefits for income in retirement.

Term	Definition
Pooled Superannuation Trust or PST	Broadly, a unit trust authorised by APRA to invest the assets of superannuation funds and other like entities.
Preliminary Report	The Panel's publication of its preliminary views — Phase one: Clearer Super choices, 14 December 2009 and MySuper 20 April 2009; Phase two: SuperStream, 22 March 2010; and Phase three: Self-managed super solutions, 29 April 2009.
Premium	In relation to insurance, the amount paid to secure insurance coverage. Generally, the premium is paid by the fund trustee to obtain insurance cover in relation to the members of the fund, but there are also personal arrangements where the member pays for their insurance directly.
Preservation age	The minimum age prescribed in the SIS Regulations at which the superannuation benefits of a fund member become available to be paid from the superannuation fund to the member, eg retirement, disability.
Public Sector Fund (scheme)	Superannuation funds that provide benefits largely for government employees or employees of statutory authorities, or are schemes established by a Commonwealth, State or Territory law.
Replacement rate	The proportion of a member's current employment income that the current value of the member's superannuation benefits would represent if paid to the member as an income stream over the member's retirement.
Retirement income	The income on which a person relies after they retire from the workforce. This includes superannuation benefits as well as the age pension and private savings.
Retirement phase	The period of a person's life, and superannuation fund membership, after they have retired from the workforce and qualify for, and may be in receipt of, superannuation benefits.
Retirement savings account (RSA)	A capital guaranteed product offered by licensed ADIs, life insurance companies and prescribed financial institutions for retirement savings as a low risk/low income accumulation account.
Reverse mortgage	A form of borrowing under which a person is advanced money and provides a portion of the equity in their home as security with the effect of reducing their equity, rather than increasing it.
Review	This Review into the governance, efficiency, structure and operation of Australia's superannuation system established by the Minister for Superannuation and Corporate Law on 29 May 2009.
Ripoll report	The 2009 report and recommendations of the Parliamentary Joint Committee on Corporations and Financial Services Inquiry into Financial Products and Services in Australia.
RSE licence	A registrable superannuation entity licence granted by APRA under the SIS Act.
RSE licensee	A trustee that is a body corporate or that is a group of individuals who hold an RSE licence.
Safe harbour	A legal protection for a superannuation fund trustee from liability to a fund member if the member directs the trustee to invest some or all of the member's account in an investment option other than the default investment strategy, so long as the trustee had conducted appropriate due diligence in relation to making the option available.
Self-insurance	Where a superannuation fund carries all or a part of the liability for the value of members' death or disability benefits (or both) (that is, from the fund's assets), rather than covering these benefits through external insurance.

Term	Definition
Self-managed superannuation fund (SMSF)	A superannuation fund that has fewer than five members, all of whom are trustees or are directors of a corporate trustee, and is regulated by the ATO and the SIS Act. No member can be an employee of another member unless they are related.
Small APRA fund (SAF)	A superannuation fund that has fewer than five members, but is not an SMSF. SAFs are required to have a professional trustee and are regulated by APRA.
Sole purpose test	The obligation under the SIS Act that a superannuation fund must be maintained by the trustee only for specific retirement purposes and a limited number of other purposes such as disablement.
Successor fund transfer	The transfer of a members' benefits from one fund to another without their consent where the trustees of both the transferring and the receiving funds agree that 'equivalent rights' are provided to the transferring members in the receiving fund after the transfer.
Superannuation Guarantee	The legal requirement under the SG Act for an employer to make contributions at least quarterly equal to a percentage (currently 9 per cent per annum) of an employee's ordinary time earnings into a superannuation fund or RSA on behalf of the employee.
SuperStream	'SuperStream' describes a package of recommendations to enhance the current 'back office' of superannuation (see chapter 9). This includes new requirements to improve the quality of data provided by employers, to allow the use of TFNs and to require the use of technology to improve processing efficiency.
Systemic transparency	Disclosure by a trustee, typically on the fund's website, of a wide range of information, including fund documents and details about fund processes and fund management, making this information available to regulators, academics, analysts, advisers and interested members.
Total Annual Expense Ratio (TAER)	A new expense measure derived from the total expenses incurred by a fund or investment option in carrying out all its activities, regardless of whether they are characterised as relating to management, administration, investment or portfolio transactions.
Trailing commissions	Commission payments structured to be paid on an ongoing basis for as long as the members remains in the superannuation product to which the commission relates.
Trust	A legal structure in which a person (the trustee) holds property on behalf of others (the beneficiaries) who are intended to benefit from the property or income of that property. A trust is the accepted legal structure for providing superannuation in Australia.
Trust deed	The legal document establishing and governing a superannuation fund. The trust deed is the source of the trustee's powers and sets out the benefits to be paid to members from the fund.
Trustee	A person or company holding property on behalf of and acting for the benefit of another party. A trustee has fiduciary duties to beneficiaries. The trustee of a superannuation fund is the entity with sole legal responsibility under the SIS Act for the management of the fund for the benefit of fund members.
Unlisted	In relation to a superannuation fund investment, an asset for which there is no formal market for listing, quotation or trading to establish the value of the asset.

Term	Definition
Voting	In relation to a superannuation fund's investments such as securities and interests in managed investment schemes, the trustee exercising, causing to be exercised or overseeing the exercise by a delegate of, voting rights in relation to the company or trust to which the security or interest relates.
www.super.gov.au	The proposed government website about superannuation to centralise information currently provided by a wide range of government websites. This central website would include standard disclosure of legislative, tax and other superannuation-related features as well as act as a portal to other superannuation information.

Notes

(a) Figures in tables and generally in the text have been rounded.

(b) The following notations are used:

$M $ million

$B $ billion

$T $ trillion

(c) The term 'Government' is used when referring to the current government and the decisions and activities made by the current Government on behalf of the Commonwealth of Australia.

(d) The term 'government' is used when referring to a past government or governments and the decisions and activities made by past governments on behalf of the Commonwealth of Australia.

APPENDIX H: BIBLIOGRAPHY AND REFERENCE MATERIAL

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APPENDIX I: SUBMISSIONS

The Panel wishes to thank all the individuals and organisations who contributed to the Review process by making a submission. The non-confidential, formal submissions can be viewed at: -<www.supersystemreview.gov.au>. The following is a list of those submissions.

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2	DEBENHAM, RAY (1)
3	BIRD, RON AND GRAY, JACK
4	ROSE, ROBERT
5	WHITE, GAVIN
6	NAME WITHHELD
7	ROMIJN, SIMON
8	MAHON, VINCENT (1)
9	TRYTELL, MORRIS
10	APPELT, MARK
11	NETHERCOTE, BARRY
12	DREW, MICHAEL
13	BAXTER, CHRIS
14	CHAPMAN, CRAIG
15	JAPHENER
16	BLACKLOW, COLIN
17	CONFIDENTIAL
18	AUSTRALIA INSTITUTE (1)
19	HICKMAN, RAY
20	AUSTRALIAN COUNCIL OF PUBLIC SECTOR RETIREE ORGANISATIONS (1)
21	GILBERT, STUART
22	HODGKINTON, NORMAN (1)
23	SUPER ADVICE SERVICES (1)
24	ASSOCIATION OF INDEPENDENT RETIREES (1)
25	COSTELLO, TERRY
26	HURR, TOM
27	MAIR, PETER
28	NSW TREASURY (1)
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30	SEMPLE SOLUTIONS (1)
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34	AXA ASIA PACIFIC HOLDINGS (1)
35	CBUS (1)
36	COUNT FINANCIAL (1)
37	CPA AUSTRALIA (1)
38	ERNST & YOUNG (1)
39	GORDON, ISABEL (1)
40	INDUSTRY FUNDS MANAGEMENT
41	INDUSTRY SUPER NETWORK (ISN) (1)
42	INSTITUTE OF ACTUARIES OF AUSTRALIA (1)
43	INSTITUTE OF CHARTERED ACCOUNTANTS IN AUSTRALIA (ICAA) (1)
44	MACQUARIE BANK (1)
45	CONFIDENTIAL
46	CONFIDENTIAL
47	CONFIDENTIAL
48	CONFIDENTIAL
49	NAME WITHHELD
50	REED, MERVIN (1)
51	SMSF PROFESSIONAL ASSOCIATION OF AUSTRALIA (SPAA) (1)
52	STATEWIDE (1)
53	SUNCORP LIFE (1)
54	TOWER AUSTRALIA GROUP (1)
55	TOWNSENDS BUSINESS & CORPORATE LAWYERS (1)
56	UNISUPER (1)
57	WARAKIRRI ASSET MANAGEMENT
58	WINSEN, JOE
59	AMP (1)
60	ASHER, ANTHONY (1)
61	AUSTRALIAN COUNCIL OF SUPERANNUATION INVESTORS
62	AUSTRALIAN INSTITUTE OF SUPERANNUATION TRUSTEES (AIST) (1)
63	BRAES, THOMAS
64	BT FINANCIAL GROUP (1)
65	CLIMATE INSTITUTE (1)
66	CORPORATE SUPERANNUATION ASSOCIATION (1)
67	DAVIS, NOEL
68	D'SOUZA, TREVOR

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69	FRASER, DEREK
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71	ING AUSTRALIA (1)
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73	LAW COUNCIL OF AUSTRALIA (1)
74	MALLESONS STEPHEN JAQUES
75	MERCER (1)
76	CONFIDENTIAL
77	NAME WITHHELD
78	CONFIDENTIAL
79	CONFIDENTIAL
80	CONFIDENTIAL
81	CONFIDENTIAL
82	CONFIDENTIAL
83	NATIONAL TERTIARY EDUCATION UNION
84	PAYNE, GERRY
85	PRICEWATERHOUSECOOPERS (1)
86	QSUPER (1)
87	REGNAN
88	SELMES, DJ (1)
89	SELMES, DJ (2)
90	AUSTRALIAN COUNCIL OF TRADE UNIONS (1)
91	GOVERNMENT EMPLOYEES SUPERANNUATION BOARD (1)
92	CONFIDENTIAL
93	CONFIDENTIAL
94	ST DAVIDS RD ADVISORY (1)
95	MLC (1)
96	AUSTRALIANSUPER (1)
97	DREW, LES
98	KERESTEN, ANTHONY
99	RETAIL EMPLOYEES SUPERANNUATION TRUST (REST) (1)
100	SIOUCLIS, E
101	CONFIDENTIAL
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111	HOBBS, PAUL
112	NAME WITHHELD
113	HEALTHY FINANCES
114	LUMSDEN, GRAEME
115	CAPITAL PARTNERS
116	HAJSZAN, W
117	CONFIDENTIAL
118	RATNAKUMAR, RATNA (1)
119	MCLINTOCK, GEORGE
120	PEACE, DARYL
121	CONFIDENTIAL
122	CONFIDENTIAL
123	SOMERVILLE, LINDSAY
124	AUSTRALIA INSTITUTE (2)
125	DOW, DAVID A
126	BROUWER, PAUL
127	CONFIDENTIAL
128	SUPER ADVICE SERVICES (2)
129	ASSOCIATION OF INDEPENDENT RETIREES (2)
130	GOLDBERG, JOHN
131	CONFIDENTIAL
132	HCF LIFE
133	AUSTRALIAN COUNCIL OF PUBLIC SECTOR RETIREE ORGANISATIONS (2)
134	CORPORATE SUPERANNUATION ASSOCIATION (2)
135	EQUIPSUPER (1)
136	ERNST & YOUNG (2)
137	INSTITUTE OF CHARTERED ACCOUNTANTS IN AUSTRALIA (ICAA) (2)
138	CONFIDENTIAL
139	NAME WITHHELD
140	PAUL CHEEVER CONSULTING
141	JENSEN, GERALD
142	CONFIDENTIAL

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150	AUSTRALIAN INSTITUTE OF SUPERANNUATION TRUSTEES (AIST) (2)
151	BT FINANCIAL GROUP (2)
152	CBUS (2)
153	CONSTELLATION
154	COUNT FINANCIAL (2)
155	COX, KEVIN
156	CPA AUSTRALIA (2)
157	CUSCAL
158	EO GROUP
159	FIRST DOLLAR SOFTWARE
160	HAMSON, DOM
161	HODGKINTON, NORMAN (2)
162	INSTITUTE OF ACTUARIES OF AUSTRALIA (3)
163	JOINT SUBMISSION: BROOKVINE, PRINCIPLE ADVISORY SERVICES AND SHED ENTERPRISES
164	KRISTOF
165	LAW COUNCIL OF AUSTRALIA (2)
166	LEGALSUPER
167	LG SUPER
168	LOWE, MARK (1)
169	MELBOURNE CENTRE FOR FINANCIAL STUDIES
170	MERCER (2)
171	MORNINGSTAR
172	NAME WITHHELD
173	CONFIDENTIAL
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177	CONFIDENTIAL
178	CONFIDENTIAL
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182	PROFESSIONAL ASSOCIATIONS SUPERANNUATION LIMITED
183	QSUPER (2)
184	QUADRANT SUPERANNUATION (1)
185	SEMPLE SOLUTIONS (2)
186	SMITH, ALAN
187	SNOWBALL GROUP
188	STATEWIDE (2)
189	SUPERCHOICE
190	SWIFT SERVICES AUSTRALIA
191	T ROWE PRICE
192	TOWNSEND, TONY
193	UNISUPER (2)
194	WA LOCAL GOVERNMENT SUPERANNUATION PLAN
195	WATSON WYATT (2)
196	CHALLENGER (1)
197	DEGABRIELE, ROSALIE
198	GOVERNMENT EMPLOYEES SUPERANNUATION BOARD (2)
199	MVISION PRIVATE EQUITY ADVISERS
200	REED, MERVIN (2)
201	RETAIL EMPLOYEES SUPERANNUATION TRUST (REST) (2)
202	CONSUMER ACTION LAW CENTRE
203	CONFIDENTIAL
204	PERPETUAL LTD
205	SMSF PROFESSIONAL ASSOCIATION OF AUSTRALIA (SPAA) (2)
206	SUPER FRINGE ADVISERS
207	AXA ASIA PACIFIC HOLDINGS (2)
208	CORPORATE SUPER SPECIALIST ALLIANCE (1)
209	MLC (2)
210	OFFICE OF THE PRIVACY COMMISSIONER
211	CHOICE
212	COMBINED PENSIONERS & SUPERANNUANT ASSOCIATION OF NEW SOUTH WALES
213	JOINT SUBMISSION: AUSTRALIAN ADMINISTRATION SERVICES, SUPERPARTNERS, PILLAR ADMINISTRATION
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219	CBA WEALTH MANAGEMENT (1)
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221	CHANT WEST
222	DAKIN, HUGH
223	DST GLOBAL SOLUTIONS
224	FINANCIAL PLANNING ASSOCIATION (FPA) (2)
225	INDUSTRY SUPER NETWORK (ISN) (2)
226	INVESTMENT & FINANCIAL SERVICES ASSOCIATION (IFSA) (2)
227	LEWIS, RUSSELL
228	SUNCORP LIFE (2)
229	SUPER COMPLIANCE SERVICES (1)
230	TOWER AUSTRALIA GROUP (2)
231	AUSTRALIAN ADMINISTRATOR SERVICES
232	CONFIDENTIAL
233	RICE WARNER ACTUARIES (1)
234	WATERS DACE PARTNERS
235	NATIONAL INSTITUTE OF ACCOUNTANTS (2)
236	JOHNSTON, ADAM
237	HOPSON, KATHRYN
238	AUSTRALIAN BANKERS' ASSOCIATION (2)
239	PATERSON, ROBERT
240	RYAN, ROBIN
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242	JACOBS, A B
243	LAUWERS, HERMAN
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245	CONFIDENTIAL
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247	DREOSTI, VIC
248	SMITH, ANDREW
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259	LBW CHARTERED ACCOUNTANTS
260	STANWAY, ADAM
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263	MAHON, J AND V (2)
264	CUMMINGS, ALLEN
265	NAME WITHHELD
266	CHIDZEY, WILLIAM
267	NAME WITHHELD
268	CONFIDENTIAL
269	JONES, WILLIAM
270	FRENCH, JOHN
271	HEBBARD, COLIN
272	PRYOR, ANNE
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274	HORSHAM, TONY
275	PAZOLLI, NICK
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282	DOBLE, ALAN
283	GOREY, JAMES
284	HAY, MONICA
285	CONFIDENTIAL
286	SUPER ADVICE SERVICES (4)
287	ERNST & YOUNG (3)
288	EVANS, DOUG
289	HEYMAN, LAWRENCE

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293	HODGKINTON, NORMAN (3)
294	HOGG, DENIS
295	MELBOURNE SMSF
296	MERCER (3)
297	TAYLOR, PAULINE
298	ASSOCIATION OF INDEPENDENT RETIREES (3)
299	AUSTRALIAN COUNCIL OF PUBLIC SECTOR RETIREE ORGANISATIONS (3)
300	BOUCHER, JEFFREY
301	CBA WEALTH MANAGEMENT (2)
302	CORPORATE SUPERANNUATION ASSOCIATION (3)
303	DEBENHAM, RAY (2)
304	DIXON ADVISORY
305	GERRIE, BRENDA
306	GLYNN, DANIEL
307	GORDON, ISABEL (2)
308	LOCAL SUPER
309	CONFIDENTIAL
310	PITCHER PARTNERS (1)
311	ROHWEDDER, JURGEN
312	SEQUAL
313	SMITH, RICHARD
314	STEVENS LAFFERTY SELLERS
315	ULTON
316	ABACUS AUSTRALIAN MUTUALS
317	AMP (3)
318	ASHER, ANTHONY (2)
319	ASSOCIATION OF FINANCIAL ADVISERS
320	ASSOCIATION OF SUPERANNUATION FUNDS OF AUSTRALIA (ASFA) (3)
321	AUSTRALIAN INDUSTRY GROUP
322	BAILEY, KYM
323	BLOORE, ANDREW
324	CPA AUSTRALIA (3)
325	DAVIES, PHIL
326	DAVIS, OWEN

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328	EQUIPSUPER (2)
329	FINANCIAL PLANNING ASSOCIATION (FPA) (3)
330	HAYDEN FINANCIAL SERVICES
331	HEY, PHILLIP
332	INSTITUTE OF ACTUARIES OF AUSTRALIA (4)
333	INTERNATIONAL UNDERWRITING SERVICES
334	JOINT SUBMISSION: ASSOCIATION OF SUPERANNUATION FUNDS OF AUSTRALIA (ASFA), AUSTRALIAN INSTITUTE OF SUPERANNUATION TRUSTEES (AIST), INVESTMENT & FINANCIAL SERVICES ASSOCIATION (IFSA), CORPORATE SUPERANNUATION ASSOCIATION
335	KINGSLEY, RANDALL
336	LAW COUNCIL OF AUSTRALIA (3)
337	LOWE, MARK (2)
338	MACQUARIE BANK (2)
339	MARKWELL, JOHN
340	MULTIPORT
341	CONFIDENTIAL
342	CONFIDENTIAL
343	CONFIDENTIAL
344	CONFIDENTIAL
345	CONFIDENTIAL
346	CONFIDENTIAL
347	CONFIDENTIAL
348	CONFIDENTIAL
349	CONFIDENTIAL
350	CONFIDENTIAL
351	CONFIDENTIAL
352	NSW TREASURY (2)
353	PARTNERS SUPERANNUATION SERVICES
354	PAULL GROUP
355	POSITIVE LIFE NSW
356	PRICEWATERHOUSECOOPERS (3)
357	PROFESSIONAL FINANCIAL SOLUTIONS (2)
358	REID, R E AND S M
359	SELMES, DJ (3)
360	SMALL INDEPENDENT SUPERANNUATION FUNDS ASSOCIATION
361	SMARTSUPER
362	SMITH AND HALL

Number	Author
363	SMSF STRATEGIES
364	SUPER COMPLIANCE SERVICES (2)
365	TAXATION INSTITUTE OF AUSTRALIA
366	TOWER AUSTRALIA GROUP (3)
367	TOWERS WATSON
368	TOWNSENDS BUSINESS & CORPORATE LAWYERS (2)
369	TRUSLOVE, ALLEN
370	UNIONS NSW (1)
371	UNISUPER (3)
372	WEBB, DONALD
373	WILLIAMS PARTNERS
374	CONFIDENTIAL
375	CONFIDENTIAL
376	OUTLOOK TAX & ACCOUNTING SOLUTIONS
377	PRICE FINANCIAL INTELLIGENCE
378	TAXPAYERS AUSTRALIA
379	TRIOLI, JOHN
380	AUSTRALIAN INSTITUTE OF SUPERANNUATION TRUSTEES (AIST) (3)
381	AUSTRALIAN SHAREHOLDERS ASSOCIATION
382	INVESTMENT & FINANCIAL SERVICES ASSOCIATION (IFSA) (3)
383	CONFIDENTIAL
384	RENNICK, BOB
385	ROBINS, TRISH
386	INDUSTRY SUPER NETWORK (3)
387	AUSTRALIANSUPER (2)
388	AXA ASIA PACIFIC HOLDINGS (3)
389	NATIONAL INFORMATION CENTRE ON RETIREMENT INVESTMENTS (2)
390	VICTORIAN GOVERNMENT
391	AUSTRALIAN COUNCIL OF TRADE UNIONS (3)
392	BT FINANCIAL GROUP (3)
393	CBUS (3)
394	CORPORATE SUPER SPECIALIST ALLIANCE (2)
395	HEFFRON CONSULTING & CAVENDISH SUPERANNUATION
396	INSTITUTE OF CHARTERED ACCOUNTANTS IN AUSTRALIA (ICAA) (3)
397	KPMG (ALL PHASES INCLUDING SMSFS)
398	CONFIDENTIAL
399	PROFESSIONAL FINANCIAL SOLUTIONS (3)

Number	Author
400	SMSF PROFESSIONAL ASSOCIATION OF AUSTRALIA (SPAA) (3)
401	SUNCORP LIFE (3)
402	EDWARDS, PETER
403	HALSTEAD, BRIAN
404	RICE WARNER ACTUARIES (2)
405	ST DAVIDS RD ADVISORY (3)
406	INVESTMENT & FINANCIAL SERVICES ASSOCIATION (IFSA) (4)
407	ESSENDON CPA DISCUSSION GROUP
408	CONFIDENTIAL
409	NAME WITHHELD
410	NATIONAL INSTITUTE OF ACCOUNTANTS (3)
411	MLC (3)
412	ING AUSTRALIA (2)
413	CONFIDENTIAL
414	AUSTRALIAN BANKERS' ASSOCIATION (3)
415	CONFIDENTIAL
416	INFRASTRUCTURE PARTNERSHIPS AUSTRALIA
417	MUSHALIK, MATT
418	WALLIS, IAN
419	GREEN, GRAEME
420	NATIONAL SENIORS ASSOCIATION
421	AUSTRALIA POST
422	NAME WITHHELD
423	NAME WITHHELD
424	NAME WITHHELD
425	NAME WITHHELD
426	NAME WITHHELD
427	NAME WITHHELD
428	NAME WITHHELD
429	GORDON MACKENZIE
430	NAME WITHHELD
431	CORPORATE SUPER ASSOCIATION
432	MERCER (4)
433	JOINT SUBMISSION (ICAA, CPA, NIA)
434	ASSOCIATION OF SUPERANNUATION FUNDS OF AUSTRALIA (ASFA) — SMSFS (4)
435	ASSOCIATION OF SUPERANNUATION FUNDS OF AUSTRALIA (ASFA) — SUPERSTREAM (5)
436	ASSOCIATION OF SUPERANNUATION FUNDS OF AUSTRALIA (ASFA) — MYSUPER (6)

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438	SMSF PROFESSIONAL ASSOCIATION OF AUSTRALIA (SPAA) (4)
439	PITCHER PARTNERS (2)
440	CBA WEALTH MANAGEMENT (3)
441	ASSOCIATION OF SUPERANNUATION FUNDS OF AUSTRALIA (ASFA) — SUPPLEMENTARY SUBMISSION (7)
442	CHALLENGER (2)
443	RICE WARNER ACTUARIES (3)
444	ING AUSTRALIA (3)
445	INDUSTRY FUNDS FORUM (2)
446	INDUSTRY FUNDS FORUM (3)
447	UNIONS NSW (2)
448	PRINDABLE, ROSS
449	QUADRANT SUPERANNUATION (2)
450	AMP (4)
451	ASSOCIATION OF WESTERN AUSTRALIAN ART GALLERIES
452	SUPER COMPLIANCE SERVICES (3)
453	WHK

APPENDIX J: PUBLISHED SPEECHES

The following speeches are available on the Super System Review website (www.supersystemreview.gov.au).

Date	Speech
8 June 2010	**The Review so far …** Stockbrokers Association Of Australia, 2010 Annual Stockbrokers Conference Jeremy Cooper, Chair, Super System Review
26 May 2010	**Super: the case for microeconomic reform** An address to the Committee for Economic Development of Australia (CEDA) Jeremy Cooper, Chair, Super System Review
18 February 2010	**A Conversation About SMSFs** 2010 SPAA National Conference Jeremy Cooper, Chair, Super System Review
12 November 2009	**Scale, Focus and Alignment** ASFA 2009 Conference: 'Super in the New Age' Jeremy Cooper, Chair, Super System Review
18 June 2009	**Observations on Retirement** ASFA Luncheon Jeremy Cooper, Chair, Super System Review

APPENDIX K: OTHER SUPERANNUATION RELATED REVIEWS

This Review has been conducted concurrently with several other super-related reviews, including:

Australia's Future Tax System Review (**AFTS**) — which reported to Government on 31 December 2009 and was responded to by Government on 2 May 2010;

- The Parliamentary Joint Committee on Corporations and Financial Services Inquiry into Financial Products and Services in Australia (**Ripoll report**) — which reported to Government on 23 November 2009 and was responded to by Government on 26 April 2010; and
- The Australian Financial Centre Forum's report, Australia as a Regional Financial Centre: Building on Our Strengths (**Johnson report**) — which was released on 15 January 2010 and responded to by Government on 11 May 2010.

This final report needs to be viewed in the context of the issues addressed by these reviews.

11.1 AFTS Review

The Henry Review was tasked with recommending improvements to the tax and transfer payment system for retirees. Consequently, these issues are beyond the terms of reference of this Review. As changes in this area have the potential to alter the superannuation system significantly, it is worth noting that the AFTS Review recommended that:

- the tax on contributions be abolished and employer contributions be treated as income in the hands of the individual, that an offset for low income earners be introduced, and the annual cap on contributions should be maintained;
- the tax rate on superannuation fund earnings should be halved to 7.5 per cent. It should also apply to capital gains (without a discount) and the earnings from assets supporting superannuation income streams. Superannuation funds should retain their access to imputation credits;
- the restriction on people aged 75 and over from making contributions should be removed. However, the work test should still apply for people aged 65 and over. There should be no restrictions on people wanting to purchase longevity insurance products from a prudentially regulated entity;
- the government should support the development of a longevity insurance market within the private sector through making available the data needed to create and maintain a longevity index, issuing long-term securities when fiscally appropriate and removing prescriptive rules in the SIS Regulations relating to income streams that restrict product innovation. This should be done in conjunction with the recommendation to have a uniform tax on earnings on all superannuation assets;
- the government should consider offering an immediate annuity and deferred annuity product that would allow a person to purchase a lifetime income;

- superannuation guarantee contributions should be paid at the same time as wages and employers should report superannuation contributions to their employees when a contribution is made;
- there should be a method of linking superannuation records, such as client identifiers like the tax file number, to make it easier for people to manage their superannuation;
- a superannuation portal where people can interact with government agencies and get information on retirement incomes should be developed. Over time this portal should evolve, subject to suitable safeguards, so that people can manage all their superannuation through one channel; and
- the preservation age for Service Pensioners should remain at 60 as it is already legislated to align with the eligibility age for that pension. An increase in the preservation age should apply to people who currently have a legislatively prescribed retirement age.

In response, the Government has announced an initial package of superannuation reforms:

- a 12 per cent SG — commencing with a 0.25 percentage point increase in 2013-14 and 2014-15, followed by 0.5 percentage point increments until the SG reaches 12 per cent by 2019-20;
- a low income earners Government contribution — from 1 July 2012. The Government will provide a contribution of up to $500 annually into the superannuation account of workers on adjusted taxable incomes of up to $37,000;
- concessional superannuation contribution caps for those nearing retirement — from 1 July 2012. Workers aged 50 and over with superannuation balances below $500,000 will be able to make up to $50,000 in annual, concessional superannuation contributions; and
- Raising the SG age limit from 70 to 75 — from 1 July 2013.

The Government also announced that it would consider the majority of recommendations further, although it has ruled out offering a Government annuity product.

11.2 Ripoll report

As the superannuation system is a component of Australia's financial system, overall changes to financial products and services regulation has implications for the superannuation system. In this regard, the Ripoll report made a number of recommendations of particular relevance to superannuation, including that:

- the Corporations Act be amended to explicitly include a fiduciary duty for financial advisers operating under an AFSL, requiring them to place their clients' interests ahead of their own;
- the Corporations Act be amended to require advisers to disclose more prominently in marketing material restrictions on the advice they are able to provide consumers and any potential conflicts of interest;
- the government consult with and support industry in developing the most appropriate mechanism by which to cease payments from product manufacturers to financial advisers;

- ASIC immediately begin consultation with the financial services industry on the establishment of an independent, industry-based professional standards board to oversee nomenclature, and competency and conduct standards for financial advisers; and
- ASIC develop and deliver more effective education activities targeted to groups in the community who are likely to be seeking financial advice for the first time.

In response, the Government announced the Future of Financial Advice reform package, which includes measures that go beyond the recommendations of the Ripoll report. Overall, the reforms are focused on improving the quality of financial advice and enhancing retail investor protection. They include:

- the introduction of a statutory fiduciary duty so that financial advisers must act in the best interests of their clients, subject to a 'reasonable steps' qualification, and place the best interests of their clients ahead of their own when providing personal advice to retail clients;
- simplifying the disclosure of advisory services provided to consumers by improving the Financial Service Guide (**FSG**);
- a prospective ban on conflicted remuneration structures, including commissions and volume based payments, in relation to the distribution and advice of retail investment products including managed investments, superannuation and margin loans. The measure does not initially apply to risk insurance. Furthermore, percentage-based fees (known as assets under management fees) can only be charged on ungeared products or investment amounts and only if this is agreed to by the retail investor;
- establishing an expert advisory panel which will review professional standards in the financial advice industry, including conduct and competency standards;
- the introduction of a product neutral ‘adviser charging’ regime, which retains a range of flexible options for which consumers can pay for advice, and includes a requirement for retail clients to agree to the fees and to annually renew (by opting into) an adviser's continued services;
- expanding the availability of low-cost 'simple advice' to provide access to and affordability of financial advice;
- enhancing the powers of the ASIC in relation to licensing and banning of individuals from the financial services industry; and
- an examination of the need for, and costs and benefits of, a statutory compensation scheme for financial services by Mr Richard St John, who has significant corporate law experience.

The majority of these reforms, including the prospective ban on conflicted remuneration structures, adviser charging regime, and statutory fiduciary duty, will commence from 1 July 2012, following the Government consulting with industry on the implementation of the reforms.

11.3 Johnson report

The Johnson report found that, as at June 2009, the Australian funds management industry had $1.2T under management and that it has the largest pool of funds under management in the Asia-Pacific region and the fourth largest in the world (this largely reflects Australia's compulsory superannuation system).

The recommendations of the Johnson report, which were largely accepted by the Government, cover a number of measures that are designed to see Australia realise its potential as a regional financial centre. For example, an increase in the pool of funds under management in Australia will benefit the superannuation industry by introducing efficiencies (through scale) and thereby lowering transaction costs. It will also encourage innovation in financial products. Easing restrictions on cross-border transactions will make a greater range of investment opportunities available.

While there is some degree of overlap between this report and the recommendations of concurrent reviews, this reflects the interconnected nature of the financial system. Where potential overlap applies, this report seeks to build on the recommendations of either the Henry Review or Ripoll Report as they specifically apply to the superannuation system. In particular, this report makes several recommendations relating to financial advice (particularly in chapters 1 and 8), the payment of contributions (chapter 9) and the development of an information portal (chapter 4). The Panel takes a different position in relation to adviser commissions in insurance from that taken in the *Future of Financial Advice* package. In chapter 5, the Panel recommends that adviser commission on insurance in superannuation be banned.