28 March 2019

Manager, Retirement Income Framework
Retirement Income Policy Division
The Treasury
Langton Crescent
PARKES ACT 2600

By email: superannuation@treasury.gov.au

Dear Sir/Madam

Re: AustralianSuper submission on the Retirement Income Disclosure Consultation Paper

AustralianSuper is pleased to provide a submission in relation to the abovenamed consultation paper.

AustralianSuper is one of Australia's largest superannuation funds and is run only to benefit its members. The best interests of our over 2 million members drive our decisions. We do not pay commissions to anyone to recommend us, nor do we pay dividends to shareholders. With over $140 billion in members' assets, our sole purpose is to assist our members achieve their best possible retirement outcomes.

AustralianSuper is very supportive of a standardised approach to disclosure. Certainly we accept that some of the complexities of financial products are difficult for a retail audience to comprehend, and a simplified measure would assist with product comparability.

In this regard, we support:

- providing members with indications as to the range of possible future outcomes;
- disclosure as to capital access levels;
- details as to available death benefits; and
- use of graphics where possible.

Despite this, we raise a number of issues with the proposed approach:

- lack of consideration of the impact of the Government Aged Pension (GAP) – which is a significant proportion of many retiree's overall income in retirement;
- reliance on future assumptions, which can be extremely subjective;
- single figure income disclosure – based on current year levels only;
- use of a downside standard deviation measure for risk assessment; and
- sensitivity of the risk measure to CPI.

This information is of a general nature and does not take into account your personal objectives, situation or needs. Before making a decision about AustralianSuper, consider your financial requirements and refer to the Product Disclosure Statement (PDS). AustralianSuper Pty Ltd ABN 94 006 457 987 AFSL 233788, Trustee of AustralianSuper ABN 65 714 394 898. Industry SuperFund logo used with permission of Industry Fund Services (IFS). This consent had not been withdrawn at the date of publication.

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These issues are described in more detail below.

Government Age Pension (GAP)

This consultation paper focuses on product disclosure; as such we note that it focuses on the individual's economic position arising out of the investment product itself. What this doesn't take into account is the outcome for the member more holistically, and in particular in light of any GAP entitlements they may have. We suggest that such disclosure is more useful to members when making decisions about retirement product selection.

For example, we believe that members may be more inclined to take investment risk where a greater proportion of their income is represented by the GAP. This is because this forms a stable secure income stream – which increases at AWOTE – providing a large component of some members' CPI protection.

Whilst this is difficult to address in a mass-customisation context, alternatives may be to provide standardised examples – e.g. full GAP entitlement, part GAP entitlement, nil GAP entitlement. The impact of the GAP is important given that the Retirement Income Covenant Position Paper – Stage one of the Retirement Income Framework (May 2018) specifically calls upon product providers to consider the GAP when designing their retirement income strategy. The paper further notes that trustees may choose to incorporate the GAP in determining "broadly constant income" in CIPR design.

Assumptions

Whilst we commend the approach of standardising risk disclosure – via the simulated income illustration and the Income Variation Risk Measure (IVRM) – we note that this is dependent on economic forecasts.

Ultimately, economic forecasts – especially over the long-term – are unavoidably unreliable. Where one party believes economic returns may be high, another may be inclined to take a more conservative approach. There are inherent conflicts between modelling based on forecasts and a standard approach. As noted, the IVRM is extremely sensitive to the investment portfolio underlying a product – and in particular the assumptions used for modelling purposes.

We know that longevity insurance pricing in Australia is expensive, given a lack of insurance experience – again, variations in assumptions can have a dramatic impact on the outcome.

In any scenario that allows for gaming, this will inevitably lead to an over-optimistic bias and/or opinion shopping.

The investment industry has always looked at standard deviation (including downside standard deviation) measures with caution. Other measures of risk are being discussed by industry practitioners that may be simpler to apply – and less subjective. In the context of investment product comparison being considered by the Productivity Commission, perhaps the two channels of discussion as to how to approach this issue should be combined.

Investment and insurance assumptions aside, products with 'guarantees' will result in low risk assessments. This assumes that all providers are the same – which credit quality would suggest otherwise. Given the long investment horizon, lack of portability and the fact that individuals are likely to be putting “all their eggs in one basket” with the guarantee provider (risk of total loss), the fact that these risks are not addressed should be a concern.

Single Figure Income Disclosure

We expect that the single figure income level is likely to be a headline figure focused on by many. Whilst additional information is presented (via the simulated distribution illustration), given the range of product design options available, there may be an over-emphasis on this headline figure.

The simulated distribution is very helpful to illustrate the range of potential outcomes a member may face, but this illustration is:

- highly dependent on underlying assumptions; and
- if only showing a 5% and 95% range – may illustrate too broad a range of outcomes. Perhaps several metrics (displayed graphically) such as – mean plus 2 standard deviations – may provide more comfort to members as to the probability of outlier outcomes.

Sensitivity to CPI

Feedback from member research suggests that spending patterns of members over time do not correlate with inflation. In particular, many retirees actual expenditure is more consistent with nominal terms, as they become less active as they age. Sub-components of CPI are more impactful – such as medical care, and the cost of aged-care facilities.

Their personal circumstances are more complex than CPI.

As the current measures show – with an indexed life annuity showing 0 risk, and a non-indexed life annuity presenting with the highest risk measure – we don’t believe this is consistent with how “risky” these products would be perceived by consumers.

As noted above, a further complexity is the impact of the GAP (indexing at AWOTE). In relation to the variations in member needs to meet their personal circumstances, other “risks” that are more important to members are considerations such as ready access to capital to meet emergency type requirements such as health and retirement living support arrangements.

Other Parameters

Some brief queries on some of the other parameters/features proposed are:

- lack of survivorship weighting in the risk measure
    - we query whether this over-emphasises remote outcomes that are unlikely to occur
- use of the age 67-97 illustration timeframe

    - if the government's policy is to promote CIPRs and tail end longevity protection, should this be extended to provide assurance for members for those long-tail longevity outcomes?
    - as retirement age is increasing, products are increasingly likely to be offered to members at different ages. If pricing is more/less expensive if acquired at a latter age, how will a member be able to assess this?
    - with improvements in digital capability, should ability to show an illustrations tailored to different ages be made available?
- Assumes a set and forget approach – what if there is the ability to adjust? How does the model address this? We are looking at approaches where it may be possible to:
    - review/update economic assumptions;
    - vary underlying investments; and
    - adjust income levels.

NEXT STEPS

We agree that consumer testing is essential before adopting any given approach and can provide some assistance in this regard if required.

If you have any questions or would like further information please do not hesitate to contact Carol Lee on [redacted] or myself on [redacted].

Yours sincerely

Louise du Pre-Alba
Strategic Policy Advocate