23 December 2020

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

Email: superannuation@treasury.gov.au

Dear Sir/Madam

Your Future, Your Super Package

The Actuaries Institute (the "Institute") supports the overarching intent of Treasury's Your Future, Your Super reforms, which is to maximise the superannuation retirement savings of Australians.

The attached documents respond in detail, providing our views on the reforms and the exposure draft legislation released on 26 November 2020. In reaching our conclusions, we have also considered the findings and recommendations from the *Productivity Commission* review into superannuation.

Our views and observations cover the following four topics:

1. Stapling of Superannuation Accounts and role of Employer sponsored funds
2. Insurance implications
3. Annual Performance Test
4. YourSuper Comparison Tool

1. Stapling of Superannuation Accounts and role of Employer sponsored funds

Employer sponsored funds have an important role to play in driving competition across the superannuation industry as they run tenders and move around. Corporate superannuation plans, including sub-plans within multi-employer industry funds and retail master trusts, often have a number of unique and strong benefits. These can include higher employer contributions, subsidised and lower fees, tailored and/or free insurance and in some cases defined benefits. In the multi-employer sub-plan segment, most larger employers will regularly review their default arrangements, or at a minimum when current performance and/or other information indicates that it may no longer be competitive.

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The corporate super segment helps to keep the superannuation environment competitive for many members and its important role should not be overlooked. In the private sector, more than 30%[1] of employees work for businesses with 200 or more employees and well over 50% for businesses with 20 or more employees (56% in 2017). For many of these employees, the workplace can be an important and efficient source of information about their superannuation funds and its performance.

To ***support the viability of Corporate Super arrangements***, given employees eligible for these arrangements will rarely be "first time" workers, we recommend that clear guidance be provided that employers are able to inform new employees of their default fund and its benefits, and that this does not trigger any advice or other legislative restrictions.

Some employees may be stapled to an employer sponsored fund which does not accept contributions from other employers. The regulations need to allow for this situation, as the employee will have an existing account balance flagged by ATO, but a new employer will not be eligible to contribute.

2. Insurance implications

The Actuaries Institute supports the provision of insurance benefits through superannuation funds for a number of public policy reasons. The Institute is concerned that the proposed Your Future, Your Super changes will negatively impact member insurance outcomes. They represent another significant change to insurance in super ahead of the review of insurance that the Government will undertake as it follows the Productivity Commission recommendations.

We have set out areas where we are ***concerned that member outcomes may be negatively impacted by the Your Future, Your Super reforms***. These concerns are that premiums rates may increase for members, that certain occupations would be denied cover and that certain benefits arranged for members would be removed.

We further recommend that the following additional data fields be provided to the trustee of a member's fund:

a) From the new Single Touch Payroll design provided to the fund on joining:
   - ANZSIC, new member type, salary and start date

b) From the ATO the member's occupation as provided to the ATO with their annual tax return.

3. Annual Performance Test

The exposure draft legislation did not include any details on the assessment requirements. Based on the proposed methodology, ***the Institute has strong concerns***, consistent with commentary released by other industry bodies, such as the Conexus Institute research[2].

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[1] https://www.aph.gov.au/About_Parliament/Parliamentary_Departments/Parliamentary_Library/pubs/rp/rp1819/SmallBusinessSector

[2] https://theconexusinstitute.org.au/resources/your-future-your-super/.

The performance test focuses on the execution of an investment strategy, not the investment strategy itself. For example, an investment strategy which wholly invests in cash is very unlikely to fail the test, however this may not produce a good member outcome. It is also possible that investment options may underperform relative to the performance test but exhibit strong relative performance on a net returns basis (i.e. YourSuper). This would be confusing for members and could further erode the credibility of the YourSuper comparison tool.

The Institute would be happy to consult further on the design of the performance test (or tests should the Government also adopt a secondary test) to be included in the Regulations. In particular, ***the Regulations should ensure that Defined Benefit plans are not impacted***.

4. YourSuper Comparison Tool

In SPS 515 – Strategic Planning and Member Outcomes, APRA requires trustees to segment their business and members into appropriate cohorts. It recognises members are different and products and offerings that are suitable for one cohort of members might not be suitable for a different cohort. This is important and should be reflected consistently in the YourSuper comparison tool by disclosing helpful information at key member segment level rather than simply at fund and product level.

We make the following key recommendations:

- At least three different levels of member age and account balance should be shown as they are the two key variables to consider in disclosing fees, and investment risk and returns. This requires collecting relevant data and information from funds applicable to nine (three times three) member segments.
- When members click into the comparison tool site, they should select their age and whether they are a new worker or existing member. Based on the information entered, the comparison tool could only disclose the information that is relevant to the members based on the identified segment the member belongs to.
- Investment returns should be presented over a long time period and also broken down into separate periods (e.g. 12 years broken down into 3 separate and independent 4 year periods).

We provide more in-depth considerations and recommendations on the implications of Stapling, Insurance and the YourSuper Comparison Tool in the attachment to this letter. We would be happy to discuss this letter or to provide further information. Please contact our CEO, Elayne Grace elayne.grace@actuaries.asn.au if you wish to clarify any aspects of this submission.

Yours sincerely

Hoa Bui
President

1. Stapling of Superannuation Account and role of employer sponsored funds

The Institute supports the Government's goal to reduce multiple unintended superannuation accounts. However, the implementation of Stapling as part of the YFYS package may have unintended consequences and result in worse member outcomes across the industry.

Stapling Implications

The Institute understands that the Productivity Commission's preferred default allocation mechanism was Assisted Employee Choice. New members, without an existing account balance and who did not elect choice, would be allocated to a shortlist, as selected by an expert panel. This expert panel replaces the employer's role in the default decision making process.

The stapling recommendation as part of the YFYS package is implemented while still requiring employers to select a default for new employees who do not have an existing balance.

1. ***New employee, no existing account balance, no choice election***: No change, joins Employer default
2. ***New employee, no existing account balance, elects choice:*** No change, member elects choice
3. ***New employees, existing account balance, no choice election:*** Change - stapled to existing fund, does not join new Employer's default fund.

This raises a number of concerns:

- There is no safeguard preventing an employee being defaulted into an underperforming fund. Given inertia caused by stapling, a member is unlikely to move subsequently.
- A fund could exhibit many years of underperformance before it fails the performance test and action can be taken to move existing members to a better performing fund.
- Funds have less incentive to improve and innovate, instead they are encouraged to chase younger members to maintain their sustainability.

Under the current stapling proposal, the majority of new members would default into a small number of funds who have been the beneficiaries of Modern Awards or Enterprise Agreements that cover workers' first jobs. In the absence of a formal selection process this creates significant advantages for those select few. More importantly, these advantages arise from the industries on which those funds focus, but not necessarily from strong performance.

Implications on the insurance benefits are considered separately in Section 2.

Special circumstances of Tailored Employer or Corporate Super

As was presented to the Productivity Commission, a number of unique and strong benefits exist in corporate superannuation plans, which are not public-offer. These can include higher employer contributions, subsidised and lower fees, tailored or free insurance and in some cases defined benefits. The corporate super segment should be supported to maintain the ongoing competitive improvement envisaged by the Productivity Commission.

While we appreciate that existing members in corporate super plans are not intended to be impacted by the stapling proposal, the change to the default arrangements will have significant impacts on the viability of these arrangements. New employees with an existing account will no longer default to the corporate employer plan, as a minority of these employees will be new to the workforce (i.e. most would already have an existing balance). The resulting reduction in the number of new members clearly results in a detrimental impact to these tailored arrangements.

Initiatives that could be implemented include:

1. Employers should be encouraged and supported to facilitate new employees joining their selected default. For example, where an employer wishes to inform employees of the selected default, on the basis that tailored insurance or higher employer contributions are available, ***clear guidance be provided that this is not treated as Advice***, or does not conflict with other restrictions (i.e. hawking).
2. Where an eligible employee uses the YourSuper comparison tool, their ***employer plan should be flagged with a separate explanation*** (for example: 'this MySuper product was selected by your employer and only employees of ABC Ltd are eligible to join. You may receive discounted fees or other tailored arrangements in this product.'). In addition, where this exists, the employee should be provided with a prompt that they are newly eligible for an employer plan and they should use the comparison tool. For example, on changing jobs, the ATO could send an email to the employee prompting them to use the tool as they are now eligible for a new employer plan.
3. Typically, when an employer elects to change service providers, the employer plan will SFT to the new Trustee. With the stapling proposal, the existing Trustee has an increased incentive not to approve an SFT, as they would wish to retain as many 'existing' account balances as possible. Guidance or support should be provided to support an employer's decision to move service providers that it relates to the entire employer plan. Without this the negotiating power of the employer is decreased.

Other Employer Concerns

Some employees may be members of funds which do not accept contributions from other employers. The regulations need to allow for this situation, as the employee will have an existing account balance flagged by ATO, but a new employer will not be eligible to contribute.

2. Insurance Implications

Superannuation Death and Disability Benefits

The Actuaries Institute supports the provision of insurance benefits through superannuation funds for a number of strong public policy reasons:

- The efficient pooling of financial risks provided is a necessary part of all modern economies. The spreading of the cost of what are unlikely but potentially very damaging random events across the participants in the pool helps to relieve the financial burden on those unfortunate enough to suffer an event. It reduces inequality within society and makes for a more efficient economy. Examples of the risks that are pooled in Australia include motor vehicle, work related accidents and illness, home, professional indemnity, health, death and disability.
- The replacement of part or all of the loss of future income on death or disablement has important social benefits as it supports financially those people who are faced with the very serious financial consequences of death of a bread winner or their own disability.
- Retirement is, in its full meaning, the permanent cessation of participation in the workforce. Retirement can be seen as both age based voluntary retirement and involuntary, unplanned retirement (death and disability). When considered through this lens, death and disability benefits form a natural and key component of superannuation as they are in effect another form of retirement benefit.
- The group risk superannuation market, providing death and disability benefits to members of superannuation funds, is very efficient and a relatively stable market (compared with other insurance markets). The efficiency is seen in the high but not uneconomic payout ratios (ratio of claims cost to premiums) that the industry provides to members, for example as reported by ASIC.

The Actuaries Institute believes consideration should be given to the implications of any changes to the superannuation system that diminish the efficient provision of death and disability benefits for members.

Impact on member outcomes - death and disability benefits

The proposed Your Future Your Super reforms impact the death and disability benefit arrangements provided inside super which we highlight below.

1. **<u>Stapling</u>**

   Occupation is a key driver of two very significant insurance factors, salary and risk of claim.

   Under the current arrangements, when a member changes occupation (and most likely employer and salary) they receive death and disability cover without underwriting in a new default fund that has a design (cover and premium) reflecting their new occupation. This is particularly the case for employer tailored subplans (of the Retail Funds and Industry Funds) and for Industry Funds that are industry based.

Under a stapling arrangement this change of occupation is not recognised (but see below for a solution to this) and the member is likely to be provided with cover that is then no longer as appropriate and a premium that may no longer reflect their risk. Of course, the overall premium paid to the insurer will likely be sustainable but stapling will create cross subsidies and inequalities within the pool that the trustee (based on current data available to it) can do little to rectify.

This issue will be significant as young Australians often enter the workforce in an occupation which is temporary and not aligned to their longer term occupation. For example, a large proportion of people enter the workforce in the retail and hospitality industries but move into other occupations on completion of their education and training.

Stapling will result in a reduction in the number of new insured members to most funds.

Stapling may also lead to higher premiums in those funds that are not the recipients of stapled members because the cost of accepting new cover will increase, either because of the need for more underwriting of lives or the acceptance of a higher level of antiselection if underwriting is not incorporated.

2. **Cessation of new members – failing the investment performance metric**

The inability of a fund to accept any new members if the fund fails the performance test would rapidly increase premiums as the pool of insured lives will diminish rapidly, increasing variability of outcomes and therefore the capital costs of the insurance policy as well as spreading the fixed costs over fewer and fewer members.

3. **Some members will be uninsurable**

Some funds exclude cover for some members e.g. those working in high risk occupations. If a person is stapled to one of these funds they will not receive cover, even if they change occupations and could have been granted automatic cover at that time. They may also have to disclose that they have been declined cover if they apply for cover at some point in the future with another fund or insurer.

4. **Tailored corporate superannuation arrangement**

Employees of many medium to large size corporates receive the benefit of tailored insurance cover. This not only results in more competitive premiums but also more tailored cover as the member's salary is known by the fund.

In addition, many employers subsidise partially or fully the employee's premium.

These benefits are only available because the members are provided with automatic cover which is dependent on the majority of employees joining the arrangement. Stapling will remove this as will the performance test if it is failed. This would be a major loss of benefit for these people.

An Opportunity to Assist Funds tailor their benefits more closely to members circumstances

The consequences discussed above can be mitigated to some extent through the provision of additional employer held data to trustees. The Actuaries Institute believes this extra data will result in significant improvements to member outcomes for insured death and disability benefits and ensure the continued efficient pooling of death and disability risk for Australians under the new arrangements.

The Actuaries Institute sees the Budget changes as an opportunity to enhance the provision of death and disability benefits within superannuation by tailoring the cover of members more closely to their individual circumstances. This will make the provision of death and disability benefits more efficient as it will help to reduce the under insurance and over insurance that is a natural consequence when trustees set designs with limited information about the member.

In particular, the provision of some additional data held by the employer and the ATO to trustees will enable trustees to address recent concerns expressed by ASIC regarding appropriate/inappropriate assignment of members to occupation categories for insurance purposes[3].

This can be achieved by:

a) The ATO supplying the member's occupation as provided to the ATO with their annual tax return.

Purpose: Insurance risk varies significantly for members in different occupations. This data will enable funds to set premiums that more closely reflect that risk of that member.

b) adding the following additional data fields in the new Single Touch Payroll / YourSuper design and providing the data to the employee's fund whenever that fund is assigned to be the recipient of SG contributions in respect of a person / employee:

1. The employee's **Australian and New Zealand Standard Industrial Classification (ANZSIC) codes**. This information is more relevant for insurance purposes than the Business Industry Codes (BIC).

Purpose: Insurance risk varies significantly for members in different occupations. This data will enable funds to set premiums that more closely reflect that risk of the member.

2. Which of the following **new member types** applies:

   a) The employee's existing fund was selected by the ATO for SG contributions from this employer

   b) The fund for SG contributions going forward was selected by the employee (through YourSuper)

   c) The fund for SG contributions going forward was set to be the employer's default fund (because the employee had no existing superannuation and did not select a fund through STP/YourSuper).

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[3] 20-309MR Trustees to improve occupational classification practices in insurance in superannuation. https://asic.gov.au/about-asic/news-centre/find-a-media-release/2020-releases/20-309mr-trustees-to-improve-occupational-classification-practices-in-insurance-in-superannuation/

Purpose: Insurance risk will vary depending on which of these three types of new member applies. This field will enable funds to set prices (and other terms) that appropriately reflect those differences in risk.

3. The employee's **current salary** for superannuation purposes with the new employer. The Actuaries Institute can assist in defining this, for example for casual employees and where the role involves significant overtime.

Purpose: Under the Your Future Your Super changes most funds will have members with a much more diverse range of occupations and salaries. It is therefore unlikely that a "one size fits all" approach to setting levels of automatic (default) insurance will meet the needs of this wider range of member cohorts.

In addition, insurance risk varies by salary level. This field will enable funds to tailor the initial levels of automatic (default) insurance more closely to individual insurance needs and tailor premiums accordingly.

4. The employee's **start date** with the employer

Purpose: This will allow funds to accurately determine when the conditions for granting cover and different kinds of cover apply. For example, the terms of cover often vary depending on the period since employment commenced.

3. YourSuper Comparison Tool

The Actuaries Institute is supportive of the idea of developing the YourSuper comparison tool which is aimed at providing members with simple and clear information to choose their MySuper product.

Based on the details provided in the Budget proposal, the comparison tool is going to "provide a quarterly updated table of simple super products (MySuper) ranked by fees and investment returns".

We would like to provide the following feedback and comments to help the YourSuper comparison tool achieve its intended objectives.

All MySuper Products

The original PC recommendation was for only the Best-In-Show list to be presented by the ATO through a comparison website, and that a list of up to 10 would be suitable to allow members to make an appropriate choice. The implications were that:

- From behavioural economics research and the industry size, 10 was an appropriate number of funds;
- The Best-In-Show list would already be set by an expert panel, so that presenting only fees and investment return would be appropriate to a member. The expert panel would assess each selected fund through a thorough and in-depth process.

Presenting a list of all MySuper products and only showing fees and investment return may result in poorer member engagement, and also unintended member outcomes.

Disclosure of fees and costs

Fee and cost structures are complex and often do not scale linearly. Members who make decisions based on disclosed fees calculated assuming a certain account balance level might potentially be misled if their actual account balance level is very different. They might think they have chosen a "low fees" product which in fact was not the case considering their actual account balance level. In this case, the simple "representative member" fees information often provided to the members might not help them make an informed and appropriate decision.

For the purpose of the comparison tool, it is almost impossible to come up with an account balance assumption that is going to be suitable for the majority of members who are likely to be using the tool. This is because the tool is intended to be used by both new members and existing members:

- New workers who need to choose their default superannuation product for the first time. In this case their account balance would be zero.
- Existing members who are informed that their current funds are underperforming, and they are directed to the comparison tool to make a decision. Their account balances could range widely from one member to another.

Ideally, fees should be calculated and disclosed based on a member's projected account balance over time to estimate the total fees to be charged over the members' lifetime. However, this approach adds complexity because of the need to explain the projection basis and to differentiate it from other projections that a fund may provide. We therefore suggest the comparison tool disclose first-year fees for at least three different account balances (say $10,000, $50,000 and $250,000) to help members compare across different MySuper offerings. This approach would be consistent with that used with the APRA "Heatmap".

The fees for an account balance of $10,000 could be the most suitable for new workers, and existing members could decide which of the three would be the closest to their actual account balance, or if they prefer, closest to their expected average account balance in the near future. To help members with this, guidance could be given such as:

Current Account Balance	**Account Balance to consider**
Less than $15,000	$10,000
$15,001 to $75,000	$50,000
More than $75,000	$250,000

We recommend that the fees and costs considered in this section of the comparison tool should only contain administration fees. The investment fees and costs should be considered as part of the disclosure of investment returns. Some recommendations about this are explained below.

Disclosure of net investment returns

Net investment return is defined by APRA as the time-weighted rate of return on investments, net of investment fees, indirect cost ratio investment costs, other investment costs and taxes on investment income, adjusted for cash flows as they occur. Net investment return is more relevant to members compared to gross investment return as the former is what will ultimately influence member outcomes.

It is proposed that the underperformance test considers investment returns over the past 8 years. It is important to disclose a statement to members such as "past performance is not reflective of future performance and there is no guarantee that your investment return will be at the level of past investment returns you considered when selecting a product".

We also suggest considering a longer period of measurement such as 12 years to appropriately reflect long-term performance of the product offerings. Below is a snapshot of how we think net investment returns and investment fees and costs can be disclosed in the comparison tool (link to the full table). This has been developed from previous discussions with APRA and industry bodies on "Investment League Tables".

Fund	Net Investment return												Current Investment fees & costs
	Last 4 years (1/7/2016 to 30/6/2020)			Previous 4 years (1/7/2012 to 30/6/2016)			First 4 years (1/7/2008 to 30/6/2012)			**12 years (1/7/2008 to 30/6/2020)**			
	Number of fu	103		Number of fu		71	Number of fu		57	Number of fu		57	
	Net Investment return pa	**Rank**	**Quartile**	**Net Investment return pa**	**Rank**	**Quartile**	**Net Investment return pa**	**Rank**	**Quartile**	**Net Investment return pa**	**Rank**	**Quartile**	
	(Note 1)	**(Note 2)**	**(Note 3)**	**(Note 1)**	**(Note 2)**	**(Note 3)**	**(Note 1)**	**(Note 2)**	**(Note 3)**	**(Note 1)**	**(Note 2)**	**(Note 3)**	
Fund A	3.7%	(6)	Q1										0.45%
Fund A1	4.0%	(3)	Q1	9.3%	(31)	Q2							0.56%
Fund A2	-0.4%	(91)	Q4	10.1%	(10)	Q1	3.0%	(30)	Q3	**4.2%**	**(32)**	**Q3**	0.37%
Fund A3	4.0%	(3)	Q1	6.3%	(63)	Q4	1.7%	(46)	Q4	**4.0%**	**(39)**	**Q3**	0.62%
Fund B	1.8%	(43)	Q2	5.1%	(68)	Q4	0.1%	(56)	Q4	**2.3%**	**(54)**	**Q4**	0.59%
Fund B1	-1.3%	(97)	Q4	8.7%	(40)	Q3	1.0%	(50)	Q4	**2.7%**	**(49)**	**Q4**	0.22%
Fund B2	-1.3%	(97)	Q4	8.7%	(40)	Q3	1.0%	(50)	Q4	**2.7%**	**(49)**	**Q4**	0.63%
Fund B3	-0.2%	(90)	Q4	7.9%	(53)	Q3							0.22%
Fund C	0.7%	(72)	Q3	8.1%	(52)	Q3	0.8%	(52)	Q4	**3.1%**	**(48)**	**Q4**	0.68%
…		…			…			…			**…**		
Fund Z2	3.7%	(7)	Q1	7.0%	(58)	Q4	3.5%	(22)	Q2	**4.7%**	**(24)**	**Q2**	0.22%
Median	**1.6%**			**9.1%**			**3.1%**			**4.4%**			**0.46%**

Note 1 " Net Investment Return pa" for a fund is the average compound rate of investment earnings for the period after deducting all investment fees, costs and taxes.

Note 2 "Rank"for a fund is the relative position of the fund's net investment return for each period compared to the rates for all the 57, 71 or 103 funds in that period. The fund with a Rank of 1 has the highest net investment return.

Note 3 If a fund has a Quartile of Q1, its return is in the top 25% of fund returns. If it is Q2, the return is in the next 25% of funds. If it is Q3, the return is in the next 25% of funds.If it is Q4 it is in the lowest 25% fo funds.

Key recommendations include:

- Showing net investment return for three separate 4-year periods and for the total 12-year period because:
  - The performance of each period is reported separately. Therefore, members can obtain an understanding of the investment performance from time-to-time without this being dominated by the most recent performance.
  - 4-year periods have been selected as we believe that consecutive 4-year periods should demonstrate the impact of any style bias in the portfolio of a particular fund and also the impact of medium-term investment cycles.
  - Trends in relative performance over the 12-year period are more evident and less dominated by the relative performance in the most recent period.
  - The volatility of actual and relative performance over the 12-year period is evident.
  - We note that the issue of survivor bias in the later periods is still an issue. We do, however, believe that, with this approach, the number of funds in each of the 4-year periods will be slightly more obvious to members.
- Including a Quartile measure with potential colour coding (similar to the APRA heatmap approach) to make the performance figures easier to understand by members and to achieve the objective of identifying broad trends in relative performance over time. For example, Fund B in the snapshot above is clearly in the bottom Quartile 4 over the full 12 years, but when you look at its progression of time it was Quartile 4 over the first 4 years and the next 4 years but improved to Quartile 2 over the last 4 years. **This Fund would probably fail any eight-year test but has then done quite well in the last 4 years.**
- We have included the expected level of investment fees and other investment costs. Importantly, we believe that this should be the level of investment fees and costs stated in the fund's PDS rather than any measure of the past level of these fees and costs. As stated

above, we believe that it is the net investment performance that should be examined when considering the investment capabilities of a fund and this is what matters to member outcomes. We do recognise however, that members might want to know what level of fees and other investment costs they will be paying to achieve their investment return. We suggest that it is the fees and other investment costs that will be charged in the future that is important in this context.

- We accept that many funds will not have a full twelve years of experience. However, most major funds would have at least eight years of experience (since MySuper was introduced) for an investment option that could reasonably be argued to represent the current investment option. Further, the fact that some funds only have four years of experience is important information for members as this will alert them to the age of the fund.
- We recognise that MySuper was only introduced in 2012, so we would (initially) have shorter than 12 years of investment performance data. In order to still have three separate periods, perhaps one way to transition from the current data limitations might be:

First year:	include 3 + 3 + 3 years	Total 9 years
Second year:	include 3 + 3 + 4 years	Total 10 years
Third year:	include 3 + 4 + 4 years	Total 11 years
Thereafter:	include 4 + 4 + 4 years	Total 12 years

- A new fund with less than four years of experience would disclose the past performance since inception with a note that clearly states say “this product only started 3 years ago and is measured on a shorter period compared to the rest of the products. As a result, relative performance in Quartile is not calculated for this product”.

Lifecycle Investment Strategies

For lifecycle investment strategies, most current products offered in the market are age dependent, and some are both age and account balance dependent. This means for the same MySuper lifecycle strategy, the past performance will be different for different cohorts of members with different ages and account balances. This also has implications for how underperformance is determined for lifecycle strategy products as the strategy might underperform for some cohorts but outperform for others. Ideally, the past performance should be disclosed based on members’ ages (and actual account balance levels for some offerings). If the comparison tool is designed to be interactive, it could show members’ current super accounts and it could also allow members to type in their age. This would allow the “right” history of the lifecycle strategy (e.g. the first 5 years in Growth and the next 7 years in Balanced) to be provided to members. However, if it is not technically possible, then it should at least show the past performance for three different age groups (say ages 20, 45 and 60) for members to compare across different MySuper offerings. For example, for age 45, the past 12 years performance disclosed for a lifecycle strategy should be the actual investment performance assuming the member started investing 12 years ago from age 33.

Age 20 could be the most suitable for new workers, age 45 is around the average age of accumulation members across the industry and age 60 could represent members closer to retirement.

For lifecycle strategy, it is important to disclose a statement to members such as "this is a lifecycle strategy which means your invested portfolio is likely to change over time with your age (and balance). Past performance is not reflective of future performance and there is no guarantee that your investment return will be at the level of past investment returns you considered when selecting a product especially where your invested portfolio is likely to change in the future. Please ensure you review this before making a decision."

Disclosure of investment risks

In addition to the past investment performance, the underlying risk of the MySuper investment options should also be communicated clearly to members. Otherwise, members would likely choose the offering with the best past investment returns without realising that the option might also be the "riskiest" in the list and what it means to their future performance.

We know that the current MySuper products in the market contain a wide range of asset allocations ranging from the more conservative end to the more growth-oriented end. This is reflective in the range of return targets set by MySuper products from CPI + 2% to 6% based on the most recent APRA quarterly MySuper statistics. There are various reasons why funds design their MySuper offering along the spectrum rather than concentrating on one end. Putting all MySuper products side-by-side with past performance without appropriate disclosure of risk associated with the return is likely, at present, to disadvantage funds that have strategically targeted a more conservative approach considering their member's risk appetite.

Based on a method commonly used by research houses, MySuper products could be grouped into say three to five broad categories. For example, these might be:

- High Growth 81% - 100% growth asset allocation
- Balanced 61% - 80% growth asset allocation
- Conservative Balanced 41% - 60% growth asset allocation
- Capital Stable 20% - 40% growth asset allocation
- Secure 0% - 19% growth asset allocation

This approach is relatively easy to understand, is familiar to many consumers and is regularly used by financial planners when advising clients on appropriate investment options. Although not perfect, it allows products with similar risk levels to be compared with each other. We recognise the existing challenge faced by the industry regarding inconsistent definitions of growth and defensive assets. The recent work by the Growth/Defensive asset categorisation working group could be a great step forward in tackling this challenge.

An alternative way of grouping could be based on the investment objectives of MySuper products. For example, products with investment objectives of about CPI + 3.5% could be grouped together. For this approach to be effective we believe that trustees would need to disclose that their investment objectives fall within a specified probability range, say 65% to 75%.

Product grouping should be accompanied by appropriate risk labelling and disclosure to members about what the underlying investment risk means to them to help them make the decision that best suits their needs. Appropriate risk labelling for each group should provide both short-term risk and long-term risk metrics to serve members with different investment horizons. The main risk metric currently disclosed to members is the Standard Risk Measure (SRM) which is the short-term risk metric. An Actuaries Institute's working group is currently working on developing a long-term risk metric (LTRM) that aims to help members to understand the risk of not meeting their long-term goals at retirement.

For members with only 5 to 10 years to retirement (age 55+), the short-term risk measure might be the most relevant and for younger members including new workers the long-term risk measure might be the most relevant. The more relevant metric (short or long term) should be highlighted to members based on their age and expected number of years to retirement. For example, "If you are a new worker, you might want to focus more on the long-term risk when choosing a MySuper product".

Under each product group, clear information should be provided to guide members to make decisions. For example, for a 55 year-old member, a statement for the CPI + 3.5% product group might be:

> "This group of MySuper products has an investment objective of about CPI + 3.5% p.a. Choosing this group of products means that you are prepared to accept a medium level of short-term fluctuation of returns. This means you might expect to experience 3 to 4 years of negative return over any 20-year period. Are you comfortable with this?"

Members should only then start comparing past performance of products once they are comfortable with the product group they select based on the disclosed information on both short-term and long-term risk.

There could be unintended consequences if investment risks are not disclosed appropriately. For example, this might force all funds to take more risk to try to be a "top performing fund" and funds might also become hesitant to de-risk for members approaching retirement to manage sequencing risk, even though it might be the appropriate thing to do.

Disclosing insurance arrangements

Insurance arrangements are not mentioned in the Budget proposal. However, we believe it is important for members to understand the implication on their insurance arrangement before deciding which superannuation provider is the right one for them.

We appreciate the possible complexity involved in insurance arrangements:

- Different funds might have different insurance offerings including types of insurance (life, TPD and income protection) and level of covers (inclusion, exclusion and level of benefits).
- Insurance premiums are dependent on a lot of different factors including the type of insurance, level of covers, the age, occupations, salary and gender.
- Different funds might have exclusions for certain occupations (in high risk categories) which means members with these occupations would not be able to get insurance covers with these funds.

Although insurance information might be difficult to disclose in a way that is both informative and simple for members and comparable across different providers, we believe that this should not be the reason to stay silent about insurance. That may lead to a lack of awareness that insurance cover is provided. Some members in specific high-risk occupation categories might not realise they could lose their insurance cover if they switch away to certain funds.

The comparison tool could be the perfect opportunity to raise awareness about insurance within superannuation. For example, a prompt to show members a message such as the following might be a good starting point:

“Do you know about your insurance arrangements with this MySuper product? We recommend you contact the fund on xxx-xxx to understand your insurance cover and premium before making a decision”.