AUSTRALIAN INSTITUTE of SUPERANNUATION TRUSTEES

SHAPING PROFIT-TO-MEMBER SUPER

Retirement Income Covenant Position Paper

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AIST Submission to Treasury

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AIST

The Australian Institute of Superannuation Trustees is a national not-for-profit organisation whose membership consists of the trustee directors and staff of industry, corporate and public-sector funds.

As the principal advocate and peak representative body for the $1.5 trillion profit-to-members superannuation sector, AIST plays a key role in policy development and is a leading provider of research.

AIST provides professional training and support for trustees and fund staff to help them meet the challenges of managing superannuation funds and advancing the interests of their fund members. Each year, AIST hosts the Conference of Major Superannuation Funds (CMSF), in addition to numerous other industry conferences and events.

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Executive summary

In brief: AIST supports a revised principle-based and flexible retirement income covenant, that should be progressed in tandem as soon as possible with a review of financial advice and a legislated objective of superannuation.

Existing retirement income products serve many retirees' needs and meet the members' best financial interest test; new products, including longevity products, must also deliver to meet individual members best interests and needs.

Funds may not collect or receive some information required for a retirement income strategy, and Government should facilitate collection of necessary data to enable funds to provide appropriate outcomes for members.

Retirement Income Framework

- AIST supports the introduction of a principles-based retirement income covenant, requiring superannuation trustees to deliver a strategy in members' best financial interest.
- Development of the covenant and associated strategies must include greater consideration for the majority of retirees who will continue to retire on a full or part pension.
    - This should involve balancing the 'need' to have retirees to spend their super, with the recognition that having adequate superannuation to spend is just as important.
- The Government can best provide the confidence needed for retirees to spend their super by committing and clearly communicating that all Australians will be able to access quality health and aged care in the later years of their life and emphasising that the age pension will continue to provide a longevity safety net.
- The move away from a product-based approach (and lack of references to a CIPR) is supported and rightly increases the focus on financial advice and guidance.
    - The Government's Quality of Advice Review should be brought forward from 2022 to progress in tandem with development of the covenant and be structured so as not to delay the covenant or the development of retirement income strategies.
    - Intra-fund advice should be expanded to include transition to retirement arrangements for the member and their spouse, and optimising entitlements to social security benefits.
- The legislated objective of the retirement income system, including the role of superannuation, should also be progressed as a priority, either prior to or at the same time as the covenant.

- The apparent assumption of the position paper that account-based pensions are not 'better products' is not correct, as they will continue to provide the most effective retirement income stream for most retirees for many years.
  - Other retirement products must be required to demonstrate that the cost of their delivery of a longevity solution is reasonable in the circumstances, and that it meets a members' best interest test.
- Support should be given to the development of longevity products and other innovative products that can be as an adjunct to account-based pensions in retirement income strategies, but they must be in members best financial interests.
  - These could include whole-of life products and group self-annuities developed by funds.

Retirement Income Strategy

- Outside of personal advice, super funds do not receive and cannot easily collect much of the information that is outlined as being required for a strategy (e.g. home ownership, relationship status, other sources of income).
- Where there is data available from different sources (e.g. ATO, ABS, APRA), the data is often inconsistent and difficult to align to the specific member base or lack accuracy and consistency to build an evidence base.
- The Government should explore measures to support the collection and use of data needed by trustees to formulate a strategy where barriers exist.
- The Government should address privacy and confidentiality considerations and provide a safe harbour.
  - Legislative constraints on the collection of this data should be removed at least 12 months prior to the requirement to have a strategy in place.

Recommendations

Recommendation 1: The development of the covenant and retirement income strategies should include greater consideration of the majority of members who will be retiring on a full or part pension over the next couple of decades.

Recommendation 2: The introduction of a covenant should be progressed in tandem with (but not delayed by):

- **-**a legislated objective of the retirement income system, including the role of superannuation; and
- consideration of the full breadth of regulatory and practical issues impacting on the quality and affordability of financial advice, particularly that related to advice for retirement.

Recommendation 3: The Government should provide an objective basis for assessing if 'better retirement products' meet members' best interest.

Recommendation 4: A supplementary requirement should be introduced to measure whether the cost of delivering a longevity solution meets the best financial interest test.

Recommendation 5: The Government should consider and amend if necessary the anti-hawking laws and retirement income strategy requirements so that super funds can proactively contact existing members to provide guidance on their retirement options.

Recommendation 6: The Government should implement the Consumer Data Right for superannuation in line with the Productivity Commission's recommendations.

Recommendation 7: The Government should explore measures to support the collection and use of data needed by trustees to formulate a retirement income strategy, including to address privacy, confidentiality, and the provision of a safe harbour. Legislative constraints on the collection of this data should be removed at least 12 months prior to the requirement to have a strategy in place.

Recommendation 8: The flexible implementation of the requirements for retirement income strategies should be permitted to allow for maturation. The requirement for a retirement income strategy should be voluntary for the first 12 months.

Recommendation 9: Previously proposed safe harbour protections, in limited circumstances, should be introduced.

Background

A principles-based retirement income covenant is supported

AIST Position
AIST supports the introduction of a retirement income covenant for superannuation trustees. The pivoting of the covenant towards a principles-based rather than product-based approach is an important step in giving superannuation fund trustees the necessary flexibility to design a retirement income strategy that is in the best financial interests of their members.

AIST made a submission in support of such a covenant in the consultations that took place in June 2018. In various submissions over many years, we have proposed that trustees be required to consider the retirement income needs of their members as part of a holistic approach to member needs and continue to do so.

Some of the comments made in our earlier submission[1] about a retirement income covenant remain relevant and these are referenced throughout this submission. However, in the earlier submission, we argued against the requirement for trustees to offer a Comprehensive Income Product for Retirement (CIPR) as a "default" retirement product, and we are pleased that the current position paper does not refer to or recommend such a mandated product.

The problem with a mandated retirement product, especially one with a longevity component, is that it does not meet the different needs and circumstances of retirees. While the position paper emphasises the policy challenges of superannuation monies that "remain unspent and become part of the person's bequest when they die", there is less consideration of the majority of current retirees whose concern is about not having sufficient retirement savings and whose superannuation runs out well before they die and will then be reliant on the age pension.

It would be fundamentally wrong to force retirees with lower account balances and possibly shorter longevity into products where they would effectively subsidise the retirement of those

[1] AIST (2018), *Response to Retirement Income Covenant Position Paper.* AIST Submission to Treasury. https://www.aist.asn.au/getattachment/Media-and-News/News/2018/Retirement-Income-Covenant-for-Trustees/20180615_submission_treasury_retinccovenant_v1-0_final.pdf.aspx

with higher account balances and higher than average life expectancy. Therefore, AIST is pleased that the position paper suggests a more flexible approach to super fund retirement income strategies.

The cost or 'risk transfer' of a product solution addressing longevity risk means is one reason why annuity-type products are generally higher cost than account-based pensions. This may be acceptable for members for whom this is appropriate but needs to be understood in the landscape of possible solutions/strategies. It also makes them unsuitable for low balance holders in many instances.

Recommendation 1: AIST calls for the development of the covenant and retirement income strategies to include greater consideration of the majority of members who will be retiring on a full or part pension over the next couple of decades.

A principles-based approach increases the emphasis on advice and guidance

The move away from a product-based approach does, however, move the focus to advice and guidance, and the need for high level principles for both the retirement income system and adoption of those principles as a strategy at fund level.

While we agree that the covenant is a key stage in the Government's retirement income framework, it is not the only stage, and we submit that greater consideration must be given to other parts of the framework.

Recommendation 2: AIST recommends that the introduction of a covenant be progressed in tandem with (but not delayed by):

- A legislated objective of the retirement income system, including the role of superannuation; and
- Consideration of the full breadth of regulatory and practical issues impacting on the quality and affordability of financial advice, particularly that related to advice for retirement.

A legislated objective for the retirement income system is needed

The Government has recognised the value of defining the role of superannuation. In the Explanatory Memoranda for the Superannuation (Objective) Bill 2016 [not proceeding], it was stated:

> *1.7 Given its importance, it is essential that future superannuation policy is guided by clear objectives. To achieve this, the Government will legislate the objective of the superannuation system in the Objective Bill. Subsidiary objectives will be prescribed by regulation.*[2]

Although the Government did not proceed with this Bill, AIST recommends that the Government recommence consideration of legislating an objective of the retirement income system, including the role of superannuation.

While the position paper mentions the suggestion by the Retirement Income Review for an objective of the retirement income system, it understates the strength with which this suggestion was made and the does not mention the review's preference for the objective to be legislated.

> ***An agreed objective is needed to anchor the direction of policy settings, help ensure the purpose of the system is understood, and provide a framework for assessing the performance of the system.***
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> …
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> *If the aim is to achieve consistency in the direction of retirement income policy and improve community understanding, the objective should be settled and not be subject to frequent change. For these reasons, it would be preferable if the objective for the retirement income system was legislated.*[3]

Meeting financial advice needs must be considered in tandem

The commentary on pages 3 and 4 of the position paper about the need for a retirement income covenant leads to the conclusion that one is needed but it does so after identifying the decisions, trade-offs and challenges that can be ameliorated by financial advice; advice the position paper notes is often not sought to navigate these issues.

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[2] Australian Government (2016), *Superannuation (Objective) Bill 2016*.
https://www.aph.gov.au/Parliamentary_Business/Bills_Legislation/Bills_Search_Results/Result?bId=r5762

[3] Retirement Income review (2020), p.27.

The position paper also refers to the ASIC consultation on impediments to the delivery of good-quality affordable personal advice, including advice for retirement and the proposed 2022 Treasury review into the quality of advice, as recommended by the FSRC.

These are all important considerations. However, the appropriate refocusing of the retirement income debate away from a product perspective (e.g., the requirement for a CIPR) means that the long-term pathway to retirement – especially guidance and advice – becomes more important. It does not make sense to deal with a retirement income covenant in isolation from the structure and provision of financial advice and guidance throughout a member's working life and into retirement.

ASIC consumer research has found that retirement income planning and growing superannuation were two of the three most common topics people had either received, or were interested in receiving, financial advice about.[4]

The Quality of Advice review should also examine the practical issues for the design and provision of cost-effective online tools and calculators to members. If these are allowed to be provided on a more flexible and real-world basis (e.g., using actual investment options and returns instead of generic options), super funds will be able to design tools that allow members to input their data and generate meaningful and cost-effective guidance to maximise members' retirement outcomes.

Rather than dealing with the covenant first and advice second, AIST strongly recommends that the Government address the covenant and removing obstacles to delivering quality advice in tandem.

While AIST recognises the importance of addressing both of these issues, the role of superannuation in the retirement income system is still developing, and it will still be 29 years (the position paper notes) before the median income earner will have $450,000 when they retire. This means that the Government is able to proceed carefully and comprehensively in addressing these issues.

AIST agrees that ensuring superannuation is for retirement income aligns with its intended purpose and avoids leaving large bequests where an individual lives to their life expectancy. However, this is not a challenge or opportunity (depending on your perspective) for a typical woman currently retiring on the median balance of $137,000.

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[4] ASIC (2019), *Financial advice: what consumers really think*, Report 627. https://asic.gov.au/media/5243978/rep627-published-26-august-2019.pdf

The implication of the position paper is that a retirement income covenant will translate into super fund retirement income strategies that encourage or require retirees to consume most of their superannuation before they die.

AIST agrees that a covenant should be structured to give retirees greater confidence to spend their superannuation. However, it should also be about ensuring retirees have adequate superannuation to spend in retirement based on their circumstances. Both perspectives underline the importance of addressing advice issues at the same time as the covenant.

The position paper is about getting retirees to spend their superannuation

Some of the issues faced by prospective retirees, such as trying to not outlive their superannuation, are precisely the opposite of the view expressed by the position paper, which is about not having retirees' superannuation outlive them.

While the position paper proposes giving trustees the flexibility to set a retirement income strategy that is suitable for their fund and products, the underlying intention is still that retirees should be encouraged to spend their superannuation by the time they die.

While AIST agrees that superannuation should be used to provide retirement income and should not be a vehicle for intergenerational wealth transfer, the means by which this occurs should be the subject of a full and public debate and be progressed in the context of a government commitment that all Australians will be able to access quality health and aged care in the later years of their life.

As the Retirement Income Review found[5], the retirees who hold on to their assets and leave significant bequests do not do so because they prioritise leaving a bequest but because of fear and uncertainty about their future (including future health and aged care costs).

All of these issues need to be progressed by the Government and is another reason why the Government needs to fast-track its advice review.

Unless the Government is able to address and resolve these conflicting perspectives between retirees and policymakers, this will undermine public confidence in the retirement income system and superannuation.

[5] Retirement Income Review (2020), p. 56

Assuming account-based pensions are not 'better products' is not correct

The position paper commences with an unexplained assumption that there is a need for "better retirement income products that provide higher retirement incomes" and goes on to state that "Future reforms will also encourage the development and offering of better retirement income products."

Given that most retirees now have access to account-based pensions (and there is a limited take up of annuity products likely due to current market conditions and pricing of these products), the unstated implication seems to be that account-based pensions can be improved upon.

While the profit-to-member industry would welcome being challenged to improve product offerings, the Government must provide an objective basis for assessing that 'better' retirement products meet members' best interests. For example, there could be a requirement to compare the total income (net of all fees) paid from such products over their lifetime to their individual members compared to the benchmark of account-based pension, and to quantify the cost of providing a longevity solution.

Recommendation 3: AIST calls for the Government to provide an objective basis for assessing that 'better retirement products meet members' best interest.

The proposed retirement income strategy principles in Box 1 provide a useful basis for fund development of a strategy for members retired or approaching retirement. However, the retirement income strategy principles should also be supplemented by a requirement to demonstrate that the cost of delivering a longevity solution is reasonable in the circumstances and meets a members best interest test. This could against the benchmark of an account-based pension.

Recommendation 4: AIST recommends that a supplementary requirement be introduced to measure whether the cost of delivering a longevity solution would meet the best financial interest test.

The focus must be on what is a 'better product' for a retiree

The Government must identify what a 'better product' looks like, not from the perspective of future impact on government revenues, but from the perspective of a retiree. What is a better product for a retiree?

While pooling using a group self-annuity framework may efficiently deliver retirement income for life, the assessment of group self-annuity given as an example provides a curious basis for determining if a product is in members' best interests. It is hard to see how a product that would lead to a worse financial outcome for possibly half of the members in the product could be considered either a reasonable trade-off by the trustee or a good outcome for retired members.

Members who have lower life-expectancy by virtue of their socio-economic status, ethnicity, or underlying health issues could feel rightly aggrieved if they were required or encouraged to join a product where they were structurally going to achieve a worse outcome than other members, and effectively subsidise those other members. While this risk could be explained in disclosures to members, it is unlikely this would provide sufficient consumer protection, particularly for members with low levels of financial literacy.

Another metric for considering the respective merit of products and product types is flexibility. For example, members of account-based pensions can generally exit their funds with three days' notice to their fund should their existing arrangements not meet their requirements or expectations. This gives members flexibility to exercise choice and change their retirement product if they see fit.

Use of account-based pension may be appropriate for all retirees

AIST Position
AIST supports the proposal in the position paper for a strategy to be formulated for all members in generality, or for cohorts of members in generality, but would be concerned if there was any broad-based expectation that longevity products would be used on a broad basis.

A mass-customised longevity product is not the preferred product for some AIST member funds. Longevity products may not be appropriate for members with low account balances and lower life expectancy. Conversely, account-based pensions may be appropriate as all or part of a product package for all fund members.

Research by the Australian Centre for Financial Studies for AIST in 2015 concluded that balances below $250,000 were best served by account-based pensions. (See Box 1) and that there was a role for them at all account balance levels.

Box 1: Extract from *Superannuation in the post-retirement phase: The search for a comprehensive income product for retirement*[6]

Ideally, trustees would have a detailed knowledge of their fund's member demographic and offer a default CIPR based on this information. Where these details are unknown trustees will have to make assumptions based what they do know of their members. Trustees may offer the following defaults based on their members' account balances:

• Balances below $100,000 – this cohort should be encouraged to use superannuation to pay off any outstanding debts. If significant funds remain, they could be invested into an ABP or withdrawn and invested outside the superannuation system. The majority of income will be delivered by the Age Pension.

• Balances between $100,000 and $250,000 – this cohort should be encouraged to invest their superannuation into an ABP. These members are unlikely to have significant savings outside the superannuation system and a large proportion of their income will come from the Age Pension. The Age Pension will provide some longevity management and savings should instead seek to augment income.

• Balances between $250,000 and $500,000 – this cohort should be encouraged to invest the majority of their superannuation in an ABP with some annuitisation to manage longevity risk. While this level of superannuation alone will not preclude members from receiving the Age Pension, this cohort is likely to have assets outside the superannuation system. As such they may not receive much income from the Age Pension, and changes to the means test will likely further limit their eligibility.

• Balances above $500,000 – this cohort should be encouraged to invest the majority of their superannuation in an ABP with some annuitisation to manage longevity risk. This level of superannuation alone does not prevent eligibility for a partial Age Pension; however, this cohort is expected to have significant assets outside the superannuation system. As such they may not receive any Age Pension until they have spent down some of their assets.

[6] Ralston, D. and Maddock, E. (2015). *Superannuation in the post-retirement phase: The search for a comprehensive income product for retirement.* August 2015: Australian Institute of Superannuation Trustees & the Australian Centre for Financial Studies. Available at: https://tinyurl.com/y7qmnyx4

Longevity products are not the magic pudding but must be in members' best interests

The management of longevity risk is an important consideration for both members and funds and AIST agrees that it should be taken into account in developing a fund's retirement income strategy. This consideration should of course take into account the extent to which their members are likely to have some or all of their longevity risk protected by the age pension.

AIST recognises the tendency of members to manage their longevity risk by withdrawing the minimum permitted amount from their account-based pension. Unfortunately, there is not an easy solution to retirees under-spending their superannuation assets, and the covenant must be constructed to set the objectives so that neither policymakers nor funds will be encouraged to force retirees into alternatives that might not be in their best financial interests. It is noted that the existing withdrawal rules already compel members to take increasingly higher percentages of their account-based pensions as they age, thus limit the amount available for bequests.

The position paper (and various papers and inquiries before it) and many members seem to hanker for the development of longevity products that deliver it all: high levels of return, reasonable fees, consistent income throughout retirement (i.e., until a member's death) and flexibility. As desirable as this is, we recognise this is very difficult where members have smaller balances. For many, an account-based pension in conjunction with income from the age pension is likely to be the best solution.

Allowing trustees greater flexibility and not mandating CIPR-like products as suggested in the position paper appears to be a way of lowering the bar to delivering such a product.

While AIST encourages the development of longevity products, including such options as deferred life annuities and group self-annuities, the Government should provide guidance on how these ambitious criteria can be met, and how "members best financial interest" can be met at an individual member level.

A watered-down version of a members best financial interest test as seems to be suggested in Box 4 is not a solution that governments should pursue.

Seeking an answer to the longevity challenge is a well-trod path but not one that has resulted in government policy clarity or widespread innovative product development:

- The 2010 Henry Tax Review recommended products that allowed a retiree to manage longevity risk but did not result in any policy change or product development.
- The 2010 Super System Review recommended not just a MySuper product but one that included "a single type of retirement income stream product chosen by the trustee and not

just cater for members in the pre-retirement phase." This product was to address longevity risks, but it too did not result in any policy change or product development.

- The 2014 Financial System Inquiry recommended a Comprehensive Income Product in Retirement (CIPR) that would address longevity risk, but it did not result in any policy change or product development. Despite its obvious parentage of this position paper (acknowledged in the previous position paper on a retirement income covenant) it is not even mentioned in the current position paper.

Another assessment of managing longevity risk was provided by the Productivity Commission in their 2018 superannuation inquiry[7]. Overall, the Productivity Commission's observations on longevity risk and longevity products identified a range of challenges (or at the very least, questions to be answered), and these remain today:

- *"Unless CIPRs are mandated (which no one suggests the policy merit of in an Australian context), adverse selection of those who have a better knowledge of their longevity than the provider will raise the price of CIPRs, decreasing their overall attractiveness."* (p.227)
- *"It is unlikely that poor judgment about longevity is the only factor underpinning impressions of poor value. That would assume that people were otherwise able to make actuarial assessments, which flies in the face of the generally low levels of financial literacy"* (p.228)
- And quoting approvingly from the RiceWarner submission*: "The exposure to growth assets [in MySuper products] will take the sting out of their longevity risk and they can then plan the balance of their retirement years with more security. This is a much smarter strategy than holding assets in lifecycle products or low-income products such as bonds or annuities"* (p.229)

By characterising the age pension as providing "a minimum amount of longevity risk management" that "may be sufficient without additional sources of longevity risk protection", the position paper downplays the importance of the age pension that provides income support to two-thirds of retired Australians.

The development of innovative products should be encouraged

The absence of widely accepted objectives of the superannuation system; problems with the provision of retirement advice on a safe and widespread basis; the lack of clarity of the policy setting for the retirement stage of superannuation for over a decade; and retiree concern about

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[7] Productivity Commission (2018), *Superannuation: Assessing Efficiency and Competitiveness*, Productivity Commission Inquiry Report. https://www.pc.gov.au/inquiries/completed/superannuation/assessment/report/superannuation-assessment.pdf

their money running out and not being able to meet health and aged care have all contributed to the limited development of alternate retirement products. Investment in a new product may be wasted if the regulatory settings change and the product must be changed to align.

While there have been some innovative retirement income solutions offered by profit-to-member super funds, it is also the case that the lack of policy clarity has also been a barrier to product development.

There are a number of innovations that could be introduced, with legislative support, to improve retirement products and transition to those products. These include:

- The expansion of intra-fund advice to include transition to retirement advice.
- The development of low-cost whole of life products that enable members to transition to retirement without having to change products upon retirement.
- Simplified and standardised processes for members to choose their key benefit features.
- The development of group self-annuities and collective defined contribution plans by super funds.

The Government should explicitly encourage innovation by super funds rather than by third parties such as manufacturers of life office annuity products, in order to maximise the returns that are provided to members and the alignment with members best interests.

Promoting the use of estimates in retirement income frameworks will improve member engagement and comprehension

The value of the guidance and advice a super fund provides to its members can be enhanced by retirement income estimates. AIST submits that the retirement income framework could be enhanced by promoting the use of estimates. Providing estimates help members think about their superannuation in terms of income rather than just a lump sum. Per our submission though we believe there a number of ways the framework around these could.

While this should be aligned with ASIC Class Order (CO 11/1227) on the use of retirement estimates, there are also a range of improvements that could be made to provide more flexibility for members as they approach retirement and during retirement.

AIST supports the following changes suggested by Cbus Super in their submission:

- Funds should be able to provide retirement income estimates more regularly to members (e.g., through their websites).
- Funds should be able to provide retirement income estimates to decumulation members.
- Retirement income estimates could provide a more personalised view and assist more informed decision making at retirement.

- Retirement income estimates should not be limited to an account-based pension and limited to providing an estimate of the first year's age pension.

Other legislative requirements should be aligned with the covenant

Many other requirements relate to the retirement stage of superannuation. The government should map all of these and consult on their future alignment with the covenant. A member's best interest test should be applied to assess whether the proposed alignment is appropriate.

An initial assessment suggests that the Design and Distribution Obligations, Member Outcomes Assessment, the anti-hawking requirements and the Consumer Data Right should be reviewed in light of the covenant.

- **Anti-hawking legislation**

While the anti-hawking legislation allows super funds to contact their existing members about retirement product information, there may be some incompatibility between the proposed requirements for retirement income strategies and the anti-hawking rules. Whilst personal advice is exempt and funds can still provide factual information, members may prefer guidance (general advice) about their retirement product options, and the anti-hawking rules may make this difficult. That is, it may be difficult to nudge members towards retirement products appropriate for their needs.

Recommendation 5: AIST recommends that the Government jointly consider the anti-hawking and retirement income strategy so that super funds can proactively contact existing members to provide guidance on their retirement options.

- **Data Consumer Right**

Consideration might be given to using the Consumer Data Right to empower members to release relevant personal and financial details to their super fund. This may be more feasible than government releasing personal information to funds, as it provides members with control over what information is released, to whom and for how long.

Industry could then focus on communicating that super funds will be better able to assist members with their retirement income strategy when they share relevant personal information. For those members not sharing this information, either through choice or disengagement, the fund might publish any assumptions being used in formulating their strategy.

This aligns with the Productivity Commission's recommendation to roll out the Consumer Data Right for superannuation, noting in recommendation 13:

> *"The Australian Government should automatically accredit superannuation funds to be eligible to receive (following member consent) information held by banks under the Open Banking Initiative. The Government should also roll out the […] Consumer Data Right to superannuation in parallel with implementation of the elevated outcomes tests"*[8]

AIST highlights that rolling out this access would facilitate trustees to gather information from its membership and in a way that respects privacy preferences from individual members. However, this would still require time to implement.

Recommendation 6: AIST recommends that the Government consider rolling out the Consumer Data Right for superannuation in line with the Productivity Commission's recommendations.

[8] Productivity Commission (2018), *Superannuation: Assessing Efficiency and Competitiveness*, Productivity Commission Inquiry Report. https://www.pc.gov.au/inquiries/completed/superannuation/assessment/report/superannuation-assessment.pdf

Retirement income strategy

The position paper proposes principles which establish requirements for trustees on formulating, reviewing, and giving effect to a retirement income strategy; a principles-based approach that allows for flexibility. AIST acknowledges the flexibility in the proposed approach on formulating a strategy and supports the recognition that a strategy can be developed for all members in generality, or for cohorts of members that each trustee may identify.

What does a retirement income strategy look like?

The position paper goes on to outline what a retirement income strategy looks like. Primarily, it should "[outline] 'how the trustee intends to assist their members' to achieve and balance key retirement income objectives".

AIST Position
AIST supports this in principle. However, how the paper proposes the strategy to be designed is broad and does not consider the operational, legal, and practical challenges of obtaining the information necessary to appropriately develop a retirement income strategy.

The proposal of a retirement income strategy feeds into a broader discussion of the elements that should inform it, including sources of income in retirement, expenditure patterns in retirement, the interaction with the other pillars of Australia's retirement income system[9], and the superannuation system's objective.

A retirement income strategy would therefore have to be informed by data that superannuation funds currently do not have access to under current legislative frameworks, for practical reasons, or privacy. In addition, a retirement income strategy would have to be informed by elements of the Quality of Advice review which are not going to be known to trustees until after the covenant takes effect.

Given these limitations, the regime will have to develop gradually for an appropriately informed retirement income strategy to be designed and implemented that captures members' needs and circumstances.

[9] "Retirement Income Review", p. 27, 2020.

Recommendation 7: AIST recommends that the Government explore measures to support the collection and use of data needed by trustees to formulate a retirement income strategy, including to address privacy, confidentiality, and the provision of a safe harbour. **Legislative constraints on the collection of this data should be removed at least 12 months prior to the requirement to have a strategy in place.**

Recommendation 8: AIST recommends a flexible oversight of the regime to allow for maturation.

The requirement for a retirement income strategy should be voluntary for the first 12 months.

Data

The position paper outlines several ways a trustee can formulate a retirement income strategy. It notes that the strategy should "identify and recognise the retirement income needs of the members of the fund […] and present a plan to build the fund's capacity and capability to service those needs." We highlight that this is a matter for additional guidance and would anticipate these matters to be addressed in further detail should the legislation pass.

A key driver in identifying the retirement income needs of members or cohorts of members of a fund is data. We have previously noted that data availability will be a challenge for trustees in formulating a retirement income strategy, and we elaborate further on what these challenges look like in the context of the proposed covenant.

Retirement expenditure

In a 2015 report on expenditure patters on retirement[10], AIST and the Australian Centre for Financial Studies (ACFS) looked at what the provision of adequate retirement income looks like.

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[10] AIST and ACFS (2016), *Expenditure patterns in retirement.* https://www.aist.asn.au/getattachment/Media-and-News/News/2016/Expenditure-patterns-in-retirement/aist_expendpatternsretirement_aug16_web.pdf.aspx

The report identified several implications for superannuation trustees in the context of a retirement income framework, noting that:

- There is a wide range of expenditure levels and cost of living;
- Expenditure does not appear to decline through retirement;
- The majority of retired households in Australia exhibit modest expenditure levels;
- The majority of retired-aged households are not saving in retirement;
- Superannuation is growing in importance for retirees[11]

In addition, when considering retirement expenditure it is useful to note how individuals draw down their superannuation in the context of the broader retirement income system, as this forms a key part of how individual behaviour may in fact impact retirement expenditure. Subsequently, this impacts choice and what products a person may choose for retirement – ultimately impacting how a trustee may approach the development of a retirement income strategy.

The Productivity Commission identified in its *Superannuation Policy for Post-Retirement Research Paper* of 2015 that "more assets are taken as income stream rollovers than lump sums […] usually in the form of an account-base pension"[12], which is drawn down relatively slowly, likely due to the management of longevity risk and aged and health care costs[13].

However, despite these findings, the Productivity Commission noted the drawbacks of the available data. In its report, it highlighted the many sources of information on, for example, drawdown behaviour – including ABS, APRA, ATO, or HILDA Survey data[14]. All sources were inconsistent and made accuracy and consistency of measurements difficult[15].

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[11] AIST and ACFS (2016), *Expenditure patterns in retirement*. https://www.aist.asn.au/getattachment/Media-and-News/News/2016/Expenditure-patterns-in-retirement/aist_expendpatternsretirement_aug16_web.pdf.aspx

[12] Productivity Commission (2015), *Superannuation Policy for Post-Retirement*. Productivity Commission. Research Paper, Vol 1, July 2015. https://www.pc.gov.au/research/completed/superannuation-post-retirement/super-post-retirement-volume1.pdf

[13] Ibid, p. 95

[14] Productivity Commission (2015), *Superannuation Policy for Post-Retirement*. Productivity Commission. Research Paper, Vol 2, July 2015. https://www.pc.gov.au/research/completed/superannuation-post-retirement/super-post-retirement-volume2.pdf

[15] Ibid, p. 240.

This illustrates a difficult picture for trustees to consider broadly without specific guidance on how to balance the wide-ranging and flexible approach of a retirement income strategy with the granular nature of what would inform such a strategy.

Due to these factors, AIST reiterates its call for the removal of legislative constraints on the collection of data at least 12 months prior to the requirement of a retirement income strategy, as well as a period of 12 months where the requirement for a retirement income strategy be voluntary.

Data sources

Considering existing data channels that trustees may refer to such as the Household, Income and Labour Dynamics in Australia (HILDA) Survey, AIST and ACFS's report on retirement income expenditure shows the limitations of using even relatively comprehensive data sets such as the HILDA Survey.

Notably, the report identifies that the HILDA Survey[16]:

> *"provides valuable data and insight into the expenditure levels and patters of Australian retiree households. However,* ***there are significant gaps in the data*** *which would improve the understanding of retirees' income needs […]* ***and aid the development of retirement income products"*** (emphasis added).

Other sources of data which may be gathered by trustees directly via its membership through surveys may provide more granular information to inform a retirement income strategy, but this exercise will require appropriate time for a useful strategy to be formulated.

Furthermore, there is the risk of trustees simply not being able to capture information or data points from cohorts of members who are historically disengaged with their superannuation. This may skew a retirement income strategy unintentionally as those that do respond may not represent all cohorts of members.

Safe harbour

AIST acknowledges and welcomes the move away from CIPRs and a mandate for default retirement products. Nevertheless, trustees will face challenges in obtaining accurate data for

[16] AIST and ACFS (2016), *Expenditure patterns in retirement*. https://www.aist.asn.au/getattachment/Media-and-News/News/2016/Expenditure-patterns-in-retirement/aist_expendpatternsretirement_aug16_web.pdf.aspx

their membership in relation to home ownership, household debt, level of Age Pension payments, retirement age and other potentially pertinent data points that would inform the design of a retirement income strategy.

No matter what the quality and depth of data a super fund can obtain about the financial position of a member, the variation of profiles on matters like household/family finances, health status, potential inheritance, attitudes to longevity risk and so on, will always mean that a strategy (or strategies) may have limited usefulness and applicability to any individual member

The risks associated with designing a broad strategy with limited data, or limited time to gather sufficient and appropriate data, may place trustees in a position where there are inadvertent breaches. For example, a well-designed retirement income strategy with poor underlying data may result in the strategy not suiting the membership or a membership cohort.

AIST notes that in the *Retirement Income Covenant Position Paper* of May 2018, there was a proposed safe harbour protection in the context of CIPRs. AIST supported this and continues to do so in the context of a more flexible and principles-based approach.

Recommendation 9: AIST recommends that the previously proposed safe harbour protection, in limited circumstances, be introduced.