Willis Towers Watson

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Director
Retirement, Advice and Investment Division
The Treasury
Langton Crescent
Parkes ACT 2600

By email: superannuation@treasury.gov.au

Dear Sir/Madam

Subject: Submission – Retirement income covenant

We are pleased to provide this submission in response to the government's position paper Retirement income covenant, released on 19 July 2021.

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Our submission

We welcome the release of the Retirement income covenant position paper (position paper) as an important step forward in the development of the retirement phase of the Australian superannuation system. We consider that the three key objectives set out by the government:

- maximisation of members' retirement income (taking into account the Age Pension)
- management of risks to the sustainability and stability of that income
- availability of some flexible access to savings during retirement

are suitable and capture the key trade-offs inherent in devising retirement strategy.

Nick Callil
Head of Retirement Solutions, Australia

Level 4, 555 Bourke Street
Melbourne
VIC 3000
Australia

T +61 3 8681 9800
D +61 9655 5163
M +61 407 662 464
F +61 3 8681 9888
E nick.callil@willistowerswatson.com
W willistowerswatson.com

Towers Watson Australia Pty Ltd
ABN 45 002 415 349 AFSL 229921

In our view, the discussion in the position paper on the future direction of the retirement income framework is particularly encouraging. While important, the retirement income covenant on its own will not be sufficient to create the change needed at a fund level to fully implement the government's intentions. We consider that there are steps that the government can take over both the short and longer term to overcome the barriers to funds acting in the manner encouraged by the position paper. We summarise these below.

Barrier or Issue	Suggested Remedy or Action
Lack of a 'retirement income' mindset	Review regulatory framework for retirement income estimates, with the aim of making them mandatory for all funds
Uncertainty over 'guided choice'	Provide (through regulatory guidance) explicit examples of acceptable use of guided choice
Risk of breaching financial advice laws	Pending review of financial advice laws, ASIC to provide explicit guidance regarding how fund can steer members into strategies without being in breach of the financial product advice laws.
Lack of available external data	Make public ATO / Centrelink data to assist funds in developing robust cohorts and to better understand membership

We elaborate of each of these in turn.

Lack of a 'retirement income' mindset

As the Retirement income review report notes[1], the superannuation system promotes a lump sum mindset throughout the accumulation phase. Shifting retirees to an 'income' or 'spending' focus in retirement phase is therefore challenging. A retirement income covenant, while an important initiative towards effecting this change, cannot do so on its own. Further initiatives are also necessary to encourage 'retirement income' thinking among fund members well before retirement.

While changing such a mindset is necessarily a long-term project, we suggest starting with a review of the regulatory framework around issuing retirement income estimates (RIEs), with the objective of making these mandatory (with sensible exclusions), rather than voluntary, for all funds. In our view, the current framework is hampered by the underlying assumption that RIEs are considered to be financial product advice that is personal advice. This situation considerably limits trustees' flexibility in providing information to encourage 'income' thinking, and indeed misconstrues the purpose of providing RIEs – that is, to entrench an 'income' mindset and illustrate an indicative level of income (allowing for the drawdown of capital), rather than to promote any particular financial product.

Uncertainty over guided choice

The position paper states that funds will be able to identify cohorts of members and identify retirement income strategies that may be appropriate for each such cohort. We support the approach outlined – indeed, we believe it reflects the approach taken by many funds already active in this area. However, the more challenging task is the implied next step – how to appropriately guide a retiree identified as belonging to a cohort towards the corresponding retirement income solution.

Even putting aside the constraints of the financial product advice laws (discussed in the next section), many retirees are either disinclined or simply not equipped to make the complex decisions associated with selecting a retirement income strategy. We strongly advocate funds being able to offer a 'fund-guided choice' framework, as described by Warren and Bell[2]. While the position paper appears to accommodate such a framework, we believe funds would benefit from the certainty that such a framework (including potentially a safety net strategy for those who do not choose) is both acceptable and consistent with the government's

[1] Retirement Income Review Final Report July 2020, 'Nest egg' framing, p 446
[2] https://theconexusinstitute.org.au/wp-content/uploads/2021/07/Ensuring-all-retirees-find-a-suitable-retirement-solution-27-July-2021-Final.pdf

retirement income objectives. This certainty could be provided, for instance, by providing explicit examples of acceptable guided choice design in regulatory guidance which would support the covenant legislation.

Risk of breaching financial advice laws

We note the government's acknowledgement in the position paper of the well-known and long-held concerns regarding the laws and regulations around providing guidance or advice to consumers including superannuation fund members. Recent developments in this area, including ASIC's consultation paper CP 332 Promoting access to affordable advice for consumers released in November 2020 and Treasury's Quality of Advice Review (QoAR) to be conducted in 2022 are welcome.

In our view, the QoAR could usefully explore a separate regulatory regime applying to guidance (including technology-enabled guidance) provided by a superannuation fund under a retirement income covenant from that applying to conventional financial advice provided by individuals or advice firms. However, we recognise this review and any resultant reform will occur over a number of years. In the meantime, we would encourage ASIC to provide guidance, in as explicit terms as possible, regarding how far, and in what manner, funds can guide retiring members into pre-determined retirement strategies with incomplete or assumed data (as is envisaged by the position paper) without being in breach of the financial product advice laws. Without the certainty provided by such guidance, we are concerned that many funds will not deviate from their current practice of offering little guidance to retiring members, which could result in retirees largely continuing to gravitate to existing retirement strategies, even where the fund has conducted the relevant analysis and is offering alternative strategies which are expected to provide better outcomes for many such retirees.

Lack of available external data

Constructing cohorts of members, which the position paper encourages, will generally require more data in relation to members than funds will hold directly. Gathering and leveraging external data will therefore be essential to developing robust and useful retirement cohorts, and more broadly is an area in which many funds are already investing to better understand their membership.

However, there is currently limited availability of relevant external data. While the position paper notes the possibility of using data from sources such as the Australian Bureau of Statistics and the Household and Labour Dynamics of Australia survey, much of this data is either not of sufficient depth or is not readily accessible.

Surveys of members by fund trustees are unlikely to solve this deficiency – given the general level of disengagement with superannuation among Australians such surveys run the risk of producing unrepresentative or unreliable data.

In our view, the process envisaged under the covenant would be greatly enhanced if there were richer sources of data available to trustees. We would therefore strongly encourage the government to consider what other sources could be made publicly available. Examples of such data could include wealth data held by the Australian Taxation Office and data on age pension payments made by Centrelink. Privacy concerns could be overcome by releasing only deidentified data or by releasing it only on a cohort basis. The better the quality and breadth of data available to trustees, the better guidance they will be able to provide to their members and therefore the better their retirement outcomes.

Finalising the covenant

We note the government's intention that subject to the passage of legislation, trustees will be required to have in place a retirement income strategy from 1 July 2022. This gives trustees less than a year to source the necessary data, identify their cohorts and develop their strategy. We would therefore encourage the government and regulators to finalise the legislation and release any supporting regulations or guidance as soon as possible. Given the new best financial interests obligations to which they are now subject, trustees may be reluctant to incur costs developing systems and processes only to find that they do not accord with the final requirements.

We would be pleased to discuss any aspect of this submission.

Yours sincerely

Nick Callil

Rose-Maree Bacon