AIST

2 May 2023

Director
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Dear Director

Your Future, Your Super Review outcomes
Superannuation Performance Test Regulations 2023

Brief

AIST welcomes the Government's review of the performance proposals to extend the time horizon of performance testing to 10 years, and its extension to some Choice products. AIST makes recommendations to improve some investment benchmarks, and the letters sent about products failing the test.

However, AIST objects to the limited and distorted way in which the performance test takes account of administration fees, and calls for it to be considered over the same time period as investments, and consistently for all superannuation products.

In addition to changes being made now, and as part of a more considered approach to regulatory change, AIST also calls for a further and more detailed review of the performance test to ensure policy objectives are being met and members interest being fulfilled.

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About AIST

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 superannuation funds.

As the principal advocate and peak representative body for the $1.7 trillion profit-to-members superannuation sector, AIST plays a key role in policy development and is a leading provider of research.

AIST advocates for financial wellbeing in retirement for all Australians regardless of gender, culture, education, or socio-economic background. Through leadership and excellence, AIST supports profit-to-member funds to achieve member-first outcomes and fairness across the retirement system.

Recommendations

Further YFYS review

- AIST recommends that there be a further and more detailed review of the YFYS performance test, and in particular, the benchmarks, over the next year, commencing with an assessment of the August 2023 performance test, to ensure the test promotes members best financial interests. This should be completed, including regulatory changes, by the first quarter of 2024.
- AIST also recommends that the further and more detailed review of the performance test address the investment and strategic management of environmental, social and governance risks (including climate change) by super funds, and the alignment of this with ESG and climate-related regulatory and legislative frameworks, and Government policy.

Lookback period for performance testing

- AIST strongly supports extending the lookback period for performance testing from 8 to 10 years as data for longer period become available, and for the comparison rankings to also align with the extended periods.

Retrospective changes to benchmarks

- AIST recommends that:
  - As a matter of principle, retrospective changes to benchmarks are not supported. However, recognising changes are proposed to resolve issues with its original iteration ahead of the August 2023 performance test, the Government should use its best endeavours to avoid making further retrospective changes to benchmarks

    (either as a consequence of a further review of covered asset classes, benchmarks and indices or the extension of performance testing to all accumulation Choice products).
  - APRA confirm there will be no requirement for the resubmission of data prior to the August 2023 performance test by super funds as a consequence of changes to benchmarks. However, where appropriate, super funds should be allowed to do so, to enable historical reporting to be aligned with the new indices.

Access to indices

- AIST recommends that Treasury initiate a process for commercially provided indices to be made available to super funds on a collective and cost-effective basis.

Recommended changes to indices

- AIST recommend that:
  - the Bloomberg AusBond Composite Bond 0+ Index be retained as the Australian Fixed Income Index.
  - the use of the Bloomberg Global Aggregate Corporate Index (hedged AUD) as the International Credit Index.
  - Treasury consult with specialist High Yield managers prior to setting the fee assumption for any future introduction of a High Yield Credit index.
- AIST recommends the development of a more representative index as the International Unlisted Property Index, and for urgent discussions with investment professionals pending implementation of the proposed new index.

Trustee notification letters

- AIST recommends that the required trustee notification letters in relation to underperforming products be improved in order to support better member comprehension and a higher level of action by members in response.

Extension of performance testing

- AIST recommends that the Government issue regulations to extend performance testing to all accumulation products and investment options, including both generic and platform products.

Scope of trustee-directed products

- AIST recommends that the grouping of covered asset classes should be extended for the purposes of determining whether a product is a trustee-directed product, by aggregating each Australian and international asset class in relation to equities, fixed income/credit, cash and alternatives.

RAFE definition

- AIST opposes the current and proposed consideration of administration fees in the performance test to fees in the most recent financial year. AIST recommends that the RAFE be based on a product's actual administration fees and expenses over the applicable lookback period, and thus be aligned with investment performance over the same period.
- AIST recommends that the benchmark administration fee (BRAFE) should be the median of all APRA-regulated accumulation superannuation products.

Legacy products

- AIST recommends that the ongoing extension of superannuation performance testing include all accumulation products closed to new members, but which have existing members.

Submission

- **Overview**

AIST supports the policy intent of the Your Future, Your Super package of reforms, and the intent of the regulation changes now proposed by Treasury (although we also believe there is scope for further important changes).

We thank the Government and Treasury for undertaking a consultation process to review the reforms, to see if they are delivering in the best interests of superannuation fund members and to identify any unintended consequences.

We note that the Government's initial response to the YFYS review relates to the annual superannuation performance test, and so this submission likewise responds to these issues and proposed changes to the YFYS regulations.

We recognise that various improvements are proposed in the proposed changes to the YFYS regulations.

However, we continue to be concerned that the policy intent of the performance testing regime is not being fully realised as a consequence of measures and metrics that the proposed regulations will still not cover the whole system, and so fail to protect many Australians from underperforming products.

While we understand the reason for the short consultation process on changes to the regulation – to identify and address unintended consequences prior to the August 2023 performance test – the speed of these changes may themselves result in unintended consequences.

We welcomed the YFYS review and called for the extension of performance testing to accumulation Choice products; testing performance over a longer period; and for the test to assess the value added by good trustee asset choice and allocation.

Many of the proposed changes to the regulations are a step in the right direction, and address these issues, and are welcomed by AIST.

These changes include extending the time period for assessment to 10 years; the partial extension of testing to Choice products; and improvements to the section 60E(6) trustee notification to beneficiaries.

Notwithstanding this comment, it remains our view that testing should be extended to all accumulation products and options, and that the notifications could be further improved.

- **Further and more detailed review of performance test**

While some of the changes to the covered asset classes and benchmarks may be an improvement, others are not, and there may also be increased complexity, cost, unintended consequences, and may still result in trustees avoiding certain investments. A range of important issues identified by stakeholders in the previous YFYS consultation have also not been addressed.

As an overall principle, the Government and regulators should carry out more post-implementation reviews of major changes to analyse their cost-effectiveness and help develop better processes for managing future changes. To this end, we welcome the announcement that a specialist policy evaluation unit will be created within Treasury.

The suitability of some benchmarks remains uncertain or debated, and the possibility of further changes and additional benchmarks adds to the uncertainty for funds.

Super funds have not been able to assess the impact of the new indices that are either not yet available or have only recently become available (eg, International Unlisted Property). This is significant from both a regulatory and a consumer protection perspective, as unintended consequences may affect investment decision-making (eg, as result of inconsistent risk profiles between related asset classes) and investment outcomes.

This uncertainty was magnified by the four-month delay in the publication of the Choice heatmap, the short time provided to consider the changes to asset classes and indices, and their retrospective application.

Although this is not ideal, we nonetheless strongly support the application on a broad basis across accumulation products, and particularly support the extension of the performance test to trustee-directed products at the earliest opportunity.

While this submission proposes some changes to indices, these proposals have been developed in a short time period, in circumstances where the impact of various indices are not known. Therefore, AIST submits that there should be a process put in place to ensure that performance testing works as it is intended.

AIST recommends that there be a further and more detailed review of the YFYS performance test, and in particular, the benchmarks, over the next year, commencing with an assessment of the August 2023 performance test, to ensure the test promotes members best financial interests. This should be completed, including regulatory changes by the first quarter of 2024.

This review should be undertaken jointly by Treasury and APRA and include consultation with investment experts across the whole of the superannuation industry. This process should include explicit and detailed alignment between meeting YFYS performance test requirements and super fund reporting to APRA.

There are also other broader and highly important issues that should be within the scope of a review. For example, many super funds take environmental, social and governance (ESG) risks, into account across their investment strategies because they are financially material over the long-term. The nature of ESG risks, such as climate change, are systemic, systematic and long-term, and the way in which consideration of these risks – and alignment with the Government's policy settings - should be taken into account in a review of the performance test.

AIST also recommends that the further and more detailed review of the performance test address the investment and strategic management of environmental, social and governance risks (including climate change) by super funds, and the alignment of this with ESG and climate-related regulatory and legislative frameworks, and Government policy.

Changes to the performance test should also follow further and ongoing extensive consultation with stakeholders, and, in line with recommendation 31 of the Financial System Inquiry. The Government and regulators should give industry participants at least six months to begin implementing regulatory changes once they are finalised, meaning that the further review should commence immediately.

A further review of YFYS should consider alternative approaches to assessment that involve accounting for Strategic Asset Allocation decisions.

In addition to this recommendation for a review, AIST makes various recommendations to improve performance test indices in the YFYS regulations.

Items 20, 21 and 49 – 10 year lookback period

AIST strongly supports extending the lookback period for performance testing as data for longer periods become available, and for the comparison rankings to also align with extended periods.

An extended lookback period provides a more reliable indicator of how funds implement their strategic asset allocation over time.

Items 3 and 48 – Table of covered asset classes

- **Retrospective changes**

Making changes to the YFYS indices, and making these changes retrospective, means they are applied retrospectively to periods during which super funds assumed in good faith that the previous regulations would apply. Retrospective benchmark changes are challenging for super funds, and result in unintended and unanticipated consequences. On a principal basis, retrospective changes are not good practice and should be avoided.

As a rule, changes to the benchmarks used for MySuper products should be prospective and should not involve restating historical performance on a different basis to that previously reported. For example, changing historic reporting of fixed income allocations could have significant performance test and member disclosure implications.

There is an increased risk of a disconnect between member communication and performance test benchmarks through increased granularity. Two funds with the same SAA in their public disclosure could have quite different performance test benchmarks.

However, we also recognise that the proposed changes to some benchmarks will occur at the same time as the expansion of the scope for the performance test to cover some Choice products, and we accept that it would also be inappropriate to have different benchmarks applying to the same asset classes for historic periods, depending on whether a product is MySuper or Choice.

AIST recommends that:

- ***As a matter of principle, retrospective changes to benchmarks are not supported. However, recognising changes are proposed to resolve issues with its original iteration ahead of the August 2023 performance test, the Government should use its best endeavours to avoid making further retrospective changes to benchmarks (either as a consequence of a further review of covered asset classes, benchmarks and indices or the extension of performance testing to all accumulation Choice products).***
- ***APRA confirm there will be no requirement for the resubmission of data prior to the August 2023 performance test by super funds as a consequence of changes to benchmarks. However, where appropriate, Funds should be permitted to do so, to enable historical reporting to be aligned with the new indices.***

- **Delay in publication of Choice Product Heatmap**

The Choice heatmap for the year ending 30 June 2022 was published by APRA on 24 April 2023, over four months later than planned. The 2021 heatmap was published using data compiled by SuperRatings, while the current heatmap was compiled using fund data reported directly to APRA.

Up until this, funds did have not had the opportunity to review APRA calculations using the data reported to APRA and to address inconsistencies and inadvertent errors. Without this opportunity and with so much data submitted there is a risk of errors and associated unintended consequences with an expansion of the performance test to Choice products this June.

Stability in the benchmarking and testing framework is necessary for good long-term outcomes. Continued changes inhibits confident risk taking and should be avoided and we would advocate for stability from here for a reasonable period.

- **Cost of indices**

Seven of the indices used to benchmark fund returns are offered by MSCI and specialised indices that are not in common use. We understand that funds may be charged between US$20,000 - $25,000 per index, whereas many other index providers make their indices available through Bloomberg at no additional cost. Noting that there are around 20 indices, this is an expensive service that offers no additional value to super funds (and ultimately is an unnecessary charge to members) given there are other serviceable indices available.

Members of the YFYS Review Technical Working Group suggested that “Index data should be transparent and free for trustees to access.” Treasury has not responded to this suggestion, and ***AIST recommend that Treasury initiate a process for commercially provided indices to be made available to super funds on a collective and cost-effective basis.***

That is, for these indices to be purchased by the Government and made available to individual super funds, on a sub-licence basis, or for equivalent and cheaper indices to be identified and substituted for the proposed indices.

Other suggestions received during our consultation with AIST member funds include removing the references to the special tax versions of the equities indices, and the use of standard indices in their place; and benchmarking global property and global property with the ANREV index of Australian property funds.

Not all of the proposed indices are available yet (or have only recently become available - e.g., International Unlisted Property). That impacts funds' ability to evaluate the impact of the new indices. This is poor practice, that will result in uncertainty, may result in unintended consequences – including outcomes that may not be in members best financial interests.

- **Recommended changes to indices**

In general, some of the changes to the benchmarks proposed in the regulations are likely to improve the performance test. However, other proposals are not positive: our submission focuses on the indices where we believe other changes should be made.

The following commentary and recommended changes to performance test indices have been developed in consultation with a working group of senior investment professionals from AIST's member funds.

  - **Australian Fixed Income Index**

In the draft regulations, the Australian Fixed Income Index is proposed to be changed from the Bloomberg AusBond Composite Bond 0+ Index ("Composite Index") to the Bloomberg AusBond Master 0+ Yr Index ("Master Index").

The rationale for this change is unclear, but we consider this change to be problematic, for the following reasons:

- We are advised by our member funds and their advisers that they are not aware of any Australian superannuation fund that uses the Master Index as the benchmark for its Australian Fixed Income portfolios. The Composite Index (or equivalent) is overwhelmingly the most common index used and best reflects the nominal fixed rate bond universe, which is the main beta investors consider when building portfolios to diversify equity risk. The fixed rate only component is in line with the most widely used global indices and would therefore seem to be the most appropriate index for the YFYS calculations.

- The Master Index includes an allocation to (typically long duration) Inflation Linked Securities which in practice are (a) highly illiquid, (b) tightly held and (c) seldom held in Australian super funds' fixed income portfolios. If even a small number of large Australian super funds were to attempt to purchase these securities to reduce YFYS benchmark tracking error, this would cause major distortions in pricing in these markets.

- Moving to the Master Index unnecessarily changes the risk-return profile of an Index which is typically used to monitor performance of stable and predictable defensive assets.
- The Master Index also includes an allocation to corporate floating rate notes. This class of securities behaves very differently from the Composite Index since it does not have any material interest rate duration, is a pure credit exposure, and tends to be more illiquid. As such, Australian super funds' fixed income portfolios do not typically group these in the same asset class, and typically benchmark them against a floating rate index.
- The Master Index was designed primarily as an index of issuance, rather than as a commonly used measure of market performance.
- Adopting the Master would mean funds are unnecessarily tracking a more complex benchmark, which would increase transaction costs for underlying members for no apparent benefit.
- Moves by superannuation funds to migrate portfolios to align with this index will incur unnecessary transaction costs for members.

AIST recommend that the Bloomberg AusBond Composite Bond 0+ Index be retained as the Australian Fixed Income Index.

- **Credit Indices**

We propose the Bloomberg AusBond Credit Index to benchmark domestic, investment grade, fixed rate credit. However, the Bloomberg Global High Yield Index is a problematic choice to benchmark international credit.

There is an inconsistency in the way that Credit indices are specified, between Australian and International. For International, a broad High Yield ("junk bond" / sub investment grade) index is used whereas for the Australian index a corporate Investment Grade index is used. The coverage and risk profiles of these indices are very different. It would be preferable for there to be consistency between the two. While we understand that Treasury chose a sub-investment grade for flexibility and as a complement to the investment grade component in the aggregate index, the majority of superannuation fund international credit allocations are investment grade, and an investment grade international credit index would be more representative of the asset class.

In practice, there are multiple forms of sub investment grade credit. These differ by sector, credit quality and duration. For example, in our experience, floating rate exposures are at least as common as fixed rate exposures within Australian superannuation funds' sub investment grade credit portfolios. Given the arbitrary focus on sub-investment grade credit, it is unclear why the proposed regulations specify a fixed rate index rather than a floating rate index or a combination of the two.

Selecting an appropriate international credit index is problematic since it ideally needs to encompass investment grade and sub investment grade cohorts across both fixed versus floating rate securities.

The preferred long-term solution would be to introduce slightly more granularity into the APRA 550 asset class classifications to differentiate between different forms of credit. However, at the present time, given the existing framework, Treasury will not be able to specify an international credit index that reflects the underlying holdings of all super funds.

AIST therefore recommend the use of the Bloomberg Global Aggregate Corporate Index (hedged AUD) for International Credit as a pragmatic solution. This would be consistent with the approach used for Australian Credit.

While the characteristics of this index differ from the proposed High Yield index and other sub investment grade floating rate indices, the overall credit quality of this index is higher than that of sub investment grade indices and would have less unintended consequences. In rough terms, the higher credit rating can be seen as an offset to the inability to specify a non-investment grade index that matches the profile of all superannuation funds' sub investment grade holdings.

If additional credit indices are to apply for sub investment grade credit and/or lower duration credit exposures, consultation on the duration and credit risk profile of portfolios (including in more conservative portfolios) would assist determining the most appropriate characteristics.

In addition, the fee assumption of 0.10% for a high yield index is unrealistic and far too low. Unlike investment-grade credit securities, it is difficult to build a passive High Yield portfolio, and the management cost of doing so would far exceed 10 basis points. AIST suggests that a fee assumption of 0.40% is more realistic.

AIST recommend that Treasury consult with specialist High Yield managers prior to setting the fee assumption for any future introduction of a High Yield Credit index.

- **International Unlisted Property Index**

The AIST investment professionals working group have identified the following concerns about the proposed International Unlisted Property Index [MSCI Global (Excl. Pan-Europe and Pan-Asia Funds) Quarterly Property Fund Index (Unfrozen) (Net Total Return; AUD fixed):

- The index appears to include Australian funds. Australian funds should not be included so as to avoid double-counting of domestic property returns and potential confusion about the appropriate disclosure of domestic versus international allocations to APRA.
- The rationale for excluding Pan-Europe and Pan-Asian funds is unclear. This may result in an index dominated by North America.
- The index permits funds with gearing of up to 60% to participate in the index. This gearing level is much higher than that of typical Australian superannuation funds. An upper limit on gearing of around 40% would be more appropriate.
- The index is unfrozen. As a general principle, frozen indices are preferred to unfrozen indices, so as to avoid survivorship bias and to avoid retrospective changes.

In addition to this, our member funds do not currently have access to this index and are concerned about decisions relating to the index being made without complete information.

AIST recommends the development of a more representative index as the International Unlisted Property Index, and for urgent discussions with investment professionals pending implementation of the proposed new index.

- **Unlisted infrastructure indices**

The current unlisted infrastructure indices are 'unfrozen', which allows for retrospective inclusion of historical returns for new index entrants, which can lead to re-stating the historical index returns. While such restatement can enable the historical index performance to better reflect the broad performance of the asset class, it can also mean that products which previously passed might fail (or vice versa).

Since the MSCI Index was included in the performance test, it has expanded coverage significantly with four additional funds and 47 additional assets added. It is unknown how many additional separate funds and mandates this would represent but indicates that the index as we understand it is close to being fully representative of qualifying funds.

The MSCI Unlisted Infrastructure Index is currently constituted of most major open-ended Australian-domiciled infrastructure funds, provides diverse asset exposure and it may be sufficiently mature to be 'frozen'. However, there may be a case for a demonstrably better and robust benchmark (including in relation to methodology re: median, average or weighted average in a lumpy asset class).

Item 53 – Trustee notification to beneficiaries

AIST remains of the view that while notification of underperformance is important, consumer choice should not be a primary mechanism to solve underperformance.

The system rather than consumers should have responsibility to achieve best member outcomes. As the Government's own analysis demonstrates, most members of underperforming funds have not responded to the letters they have been sent, and their accounts remain in underperforming funds.

As AIST has consistently submitted, members of products that fail the performance test twice should be moved under an APRA-supervised process to a MySuper product that passes the performance test, and the twice failed product closed.

Notwithstanding this, the redrafting of the required trustee notification letters in relation to underperforming products, and the extension of the requirement to send these letters to underperforming Choice products, is welcomed.

However, AIST submits that further improvements could be made to strengthen and focus the communication to members, and for these to be focus group tested with typical members prior to the next round of performance test notifications.

In the event the Government continues to leave it up to members to move from underperforming products, ***AIST recommends that the required trustee notification letters in relation to underperforming products be improved in order to support better member comprehension and a higher level of actions in response.***

The text suggested in Appendix A of this submission for MySuper products respectively has not been focus group tested but provides a possible indication of changes that could be made (with similar changes also made to notification relating to underperforming Choice products).

Items 8, 9, 10, 11 and 12 – Meaning of trustee-directed products

The extension of performance testing to trustee-directed products is supported.

AIST also supports the extension of performance testing to all accumulation products and investment options, both generic and platform products, and notes that although such testing is the intention of the primary Your Future Your Super legislation, the proposed regulations do not support this further extension.

AIST recommends that the Government issue regulations to extend performance testing to all accumulation products and investment options, both generic and platform products.

The definition of trustee-directed products is also supported, including for these products to cover strategic asset allocations to more than one asset class.

We also agree that what constitutes an asset class and appropriate grouping of asset classes should be prescribed in the regulations.

Item 12 provides rules to allow certain covered asset classes to be treated as one asset class for the purposes of working out whether a product is a trustee-directed product.

In summary, proposed sub regulation 9AB.2(4) groups international equities, Australian fixed interest credit, international fixed interest credit and alternatives as four grouped asset classes.

This will assist trustee-directed products being multi-sector accumulation products that "are most comparable to MySuper products, which enables APRA to make comparisons between outcomes received by MySuper members and choice members."[1]

AIST recommends that the grouping of covered asset classes should be extended for the purposes of determining whether a product is a trustee-directed product, by aggregating each Australian and international asset class in relation to equities, fixed income/credit, cash and alternatives.

This can be given effect by deleting proposed sub regulation 9AB.2(4) and inserting the following in its place:

(4A) Despite sub regulation (4), for the purposes of subparagraph (2)(b)(i), treat the covered asset classes for a quarter listed in each of the following paragraphs as each being one covered asset class for the quarter:

(a) the covered asset classes identified in items 1, 2, 3, 4, 5, 6 and 7 of the table in regulation 9AB.17;

(b) the covered asset classes identified in items 16, 17, 18, 20 and 21 of that table;

(c) the covered asset classes identified in items 22 and 23 of that table;

(d) the covered asset classes identified in items 24, 25 and 26 of that table.

The approach recommended by AIST is consistent with APRA's proposed segmentation of the choice sector; its schedule for extending the scope of increased transparency to more Choice products and options; and intended alignment with Your Future Your Super measures[2].

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[1] APRA Choice heatmap information pack May 2021, presented to AIST 2 June 2021.

[2] APRA Choice heatmap information pack May 2021, presented to AIST 2 June 2021.

This approach to segmentation is also aligned with definitions in APRA's Superannuation Reporting Form SRF 605.0 developed during phase 1 of its Super Data Transformation program.

At a practical level, this also reduces the prospect of unnecessary complication. For example, Australian equity indices may include some New Zealand components, and the International Unlisted Property Index includes Australia.

Items 5, 7, 13 and 46 – Meaning of representative administration fees and expenses or RAFE

The impact of administration fees should be appropriately and completely considered in the determination of product performance, but neither the current nor the proposed changes to the regulations meet this requirement.

The proposed changes to the regulations do not substantially change the use of the last financial years administration fee in the formula for the performance test (i.e., RAFE) in test formula. This continues to distort the performance test away from the *actual* net benefit delivered to members by using the existing manufactured and inaccurate basis of calculation.

Consideration of administration fees and costs should align to the actual net member benefit across the lookback period as it is extended to 10 years.

Superannuation is a long-term investment; investment performance is assessed over a longer-term; and administration fees impact on net returns. AIST believes a change to the calculation of the RAFE is an important omission that should be rectified in the proposed changes to the regulations.

AIST recommends that the RAFE should be based on a product's actual administration fees and expenses over the applicable lookback period, and thus be aligned with investment performance over the same period.

AIST strongly opposed the benchmark RAFE being calculated separately for MySuper products and TDPs in our response to the September 2022 YFYS consultation paper and continues to do so.

The benchmark administration fee (BRAFE) should be the median of all APRA-regulated accumulation superannuation products, and there should not be separate administration fees for MySuper products, Trustee Directed Products, and other choice products. The policy aim should be to avoid having higher benchmarks for non-MySuper products that will act to entrench higher fees across the choice sector.

AIST recommends that the benchmark administration fee (BRAFE) should be the median of all APRA-regulated accumulation superannuation products.

Items 5, 19, 34, 36, 38 and 40 – Meaning of index

AIST supports standardising the definitions in the regulations.

Items 1, 5, 19, 47 and 48 – Alternative asset class

AIST supports the alignment of the regulations with APRA reporting standards.

Items 24 and 27 – Calculation of 'actual return' where a trustee-directed product has 2 or more net investment returns

AIST supports the rules for determining actual return that incentivises funds to reduce investment fees on their highest fee pathways.

Items 2, 4, 6 and 8 – Definitions of asset allocation standard, fees standard, investment performance standard, and RSE structure standard

AIST supports the alignment of the regulations with APRA reporting standards.

Items 50, 51 and 52 – Application and transitional provisions

AIST supports the amendments made by the proposed regulations (subject to the comments made by AIST in this submission) applying on or after 1 July 2023.

Legacy products

In discussion with Treasury, we were also asked our view about whether the performance test should include closed Choice products and replied that it should. This is a longstanding view of AIST, and a view unequivocally supported by the recently released 2023 Choice Heatmap.

The 2023 heatmap shows that Choice products closed to new members are more likely to underperform and have higher fees that those that are open. These closed products hold $17 billion. This was identified by APRA as one of the key insights of the 2023 Choice heatmap.

Two-thirds of Choice investment options that are closed to new members had poor or significantly poor performance relative to the heatmap benchmarks. The average annual administration fee for members with an account balance of $50,000 in closed Choice products was $225, compared with $149 for open Choice products and $137 for MySuper products.[3]

APRA has stated that:

RSE licensees must demonstrate how retaining members in underperforming closed investment options remains in members' best financial interests or take active steps to identify suitable better performing options or products for these members to be transferred to.[4]

It is also the case that funds that fail the performance test twice are unable to accept new members. It would be ludicrous to suggest that because they are closed to new members, they are legacy products that should not be subject to future performance assessment.

This is also a strong argument for including legacy products in scope for the performance test.

AIST recommends that the ongoing extension of superannuation performance testing include all accumulation products closed to new members, but which have existing members.

For further information regarding our submission, please contact AIST Senior Policy Manager David Haynes at dhaynes@aist.asn.au

Yours sincerely,

Eva Scheerlinck

Chief Executive Officer

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3 https://www.apra.gov.au/news-and-publications/apra-increases-transparency-of-choice-super-products-latest-heatmap

4 https://www.apra.gov.au/news-and-publications/apra-increases-transparency-of-choice-super-products-latest-heatmap

Appendix A – indicative content for trustee notification to members if a MySuper product fails the performance test

Dear [member name],

The XYZ Super MySuper product has failed the Australian Government's annual performance test.

You should now move your superannuation to a better performing super product.

Your money will stay in your XYZ Super MySuper account unless you move it, but moving to another superannuation account is easy and costs nothing.

You could save thousands of dollars more for your retirement by switching to a better superannuation account. By earning 1% more each year for 30 years, you could retire with 20% more in savings.

You had $XXX,XXX invested in a XYZ Super MySuper account on 30 June 2023. Last financial year you paid a total of $XXX in fees to XYZ Super for that product.

The Australian Government tests many superannuation products every year to make sure they pass a performance test.

Finding a better superannuation product is easy with the Australian Government's YourSuper comparison tool. You can use the comparison tool to compare the fees and earnings of all simple, low-cost MySuper products. Go to *ato.gov.au/yoursuper* or use the QR code below:

You can contact a superannuation fund to open a new super account, and then ask it or use myGov to move your money over to your new account.

<u>Your questions answered</u>

What is the annual superannuation performance test?
Every year, the Australian Government test checks how much your superannuation account has earned for you (after fees) over the last 8/9/10 financial years. It compares earnings paid into your account with those of a similar product over the same period.

You can find out more about super at *moneysmart.gov.au*

How do I move to a new superannuation account?
The first step is to find a new superannuation product.

You should think about your investment plans and personal situation, including insurance, when moving superannuation.

You may find it helpful to use the Australian Government's YourSuper comparison tool. You can use the tool to compare the fees and earnings of simple, low-cost *MySuper products*.

Once you have chosen a new superannuation product, contact the fund to open a new account.

After opening a new account, move your money from your existing one.

You can contact the new fund or use myGov to move your superannuation. Find out more at *moneysmart.gov.au*

What happens if a superannuation product fails two or more years in a row?
If a superannuation product fails the test at least two years in a row, it cannot accept new members until it passes a future test.

This may affect the underperfoming superannuation product's ability to improve.

Your money will stay in your underperforming superannuation account unless you move it.

This letter does not take your personal situation into account. Consider your investment plans and personal situation, including insurance, when moving your superannuation.