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MAKE TOMORROW, TODAY

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Subject: CONSULTATION PAPER 249: Remaking ASIC class order on generic financial calculators

Dear Mr Christie

Mercer welcomes the opportunity to comment on Consultation Paper 249.

Executive summary

Mercer strongly recommends that the Class Order be updated rather than being allowed to sunset.

In order to properly engage with and educate superannuation fund members, further flexibility is required. Some examples of areas where greater flexibility would assist include

- Enabling providers to reference particular products/investment options as an example of the products for which the calculator and its assumptions are appropriate.

- Allowing calculators to be readily provided for situations where there is a specific product involved (for example, a particular employer's defined benefit fund)

The education of consumers would also be enhanced if calculators provided an indication of the range of uncertainty in the calculation outcomes.

Although we support a mandated assumption in relation to converting retirement estimates to current values, we do not support the mandating of other assumptions.

We believe our recommendations will ultimately lead to better informed, engaged and empowered customers.

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We have set out our responses to the questions in Section B of the consultation paper in Appendix 1.

Set out below are further comments which are not specifically covered by the Section B questions.

Levels of uncertainty

It is important for consumers to be aware that any retirement estimate, is purely that – an estimate based on the assumptions adopted.

We believe there is an education opportunity here to require calculators to provide a variability or uncertainty measure.

There are numerous means of providing such a measure ranging from basic to very sophisticated. The Actuaries Institute has issued Practice Guideline 499.02 which includes examples of some approaches which could be adopted.

Recommendation 1

The Class Order should require calculators to show an uncertainty measure.

Mandating assumptions

To avoid being misleading, it is important that providers be allowed to adopt assumptions which best reflect the particular circumstances. For example, investment returns should take into account:

- The particular investment strategy of the type of product which is being considered (including allowance for the likely investment mix, passive/active strategy etc)
- The relevant tax impact on the relevant type of product

Similarly fees and costs should reflect the likely costs (rather than being mandated by ASIC).

It is also important that providers are not restricted to using return targets or fees as reported on product dashboards as these are based on a member with a $50,000 account balance and may be inappropriate or misleading for consumers in other circumstances.

Similarly, we are concerned with the potential application of Section 29QC(1) of the Superannuation Industry (Supervision) Act 1993. Mandating the use of fees, expressed in a particular manner for another purpose, is inappropriate for the purposes of a calculator.

> ***Recommendation 2***
>
> ***Assumptions, other than an assumption to convert estimates to current values, should not be mandated. Further, Section 29QC of SIS should not apply in relation to generic calculators.***

Specific products

There are some products which would be difficult to class as generic. In the superannuation field, these would include defined benefit arrangements for a specific employer and various products which may include guarantees or some form of longevity protection. A particular issue faced by providers in this case is the requirement in the current Class Order to enable the user to change pre-populated product specific data (e.g. the user's accrued defined benefit multiple) or product-specific parameters (e.g. a guaranteed proportion of capital returned). It is important such products are not excluded from providing calculators under the terms of the Class Order so that members of such products can also be provided with relevant education tools.

> ***Recommendation 3***
>
> ***The Class Order should clarify calculators can be provided in cases where the product may not be generic and remove the requirement to allow users to change pre-populated data in such cases.***

Who is Mercer?

Mercer is a global consulting leader in talent, health, retirement and investments. Mercer helps clients around the world advance the health, wealth and performance of their most vital asset – their people.

Mercer Australia provides customised administration, technology and total benefits outsourcing solutions to a large number of employer clients and superannuation funds (including industry funds, master trusts and employer sponsored superannuation funds). We have over $50 billion in funds under administration locally and provide services to over 1.3 million super members and 15,000 private clients. Our own master trust in Australia, the Mercer Super Trust, has around 230 participating employers, 213,000 members and $19 billion in assets under management.

Mercer provides one of the most sophisticated calculators available in the Australian market to members of the Mercer Super Trust and to members of various other superannuation funds which have accepted the merits of our calculator.

Yours sincerely,

Dr David Knox
Senior Partner

APPENDIX 1: RESPONSE TO SPECIFIC QUESTIONS

B1Q1 Do you agree with these proposals? If not, why not?

a) We support the introduction of layered disclosure. This improves the consumer's ability to understand key information at junctures where it is most appropriate for their needs whilst facilitating the reduction in wordiness and congestion of the introduction screens of our calculators.

Recommendation B1a
The updated Class Order should enable the use of layered disclosure.

b) We support a requirement to adjust medium-long term results for inflation. See response to B1Q5

Recommendation B1b
Medium-Long term results should be adjusted for inflation.

c) We support the introduction of mandatory self-reporting of breaches as this requires non-AFSL holders to meet the standards of AFSL holders.

However, we **do not** support the proposal of reporting "likely breaches". Such a requirement would add red tape whilst not assisting or protecting consumers in any discernible manner. We also expect there would be considerable difficulties in trying to define what is meant by a "likely breach" and considering whether a "likely breach" report has been triggered.

Instead we advocate a more appropriate quality control mechanism would be to require any such calculator to be "signed-off" by an actuary. (The Actuaries Institute has issued Practice Guideline 499.02: Projected Superannuation Benefit Illustrations.) In our view this achieves the policy objective of the proposal whilst minimising red tape.

Recommendation B1c(i)

Mandatory self-reporting should be required by non-AFSL holders to ensure consistent treatment.

Recommendation B1c(ii)

Self-reporting of likely breaches should not be required for AFSL and non-AFSL holders.

Recommendation B1c(iii)

The Class Order should include a requirement for any generic calculator to be "signed off" by an actuary.

d) We understand ASIC proposes to clarify that "the assumptions used by a calculator may in fact reflect a particular financial product" however the calculator "should not refer to any particular product".

We have significant concerns in respect of this limitation, as in our view, it is not user friendly and will make it more difficult for consumers to understand the output and learn from the results.

In particular, consider a situation where a consumer is considering different investment strategies. In order to provide reasonable generic advice, it will be necessary for calculators to use different investment return assumptions with the assumptions depending on the investment strategy adopted. In other words, different assumptions will be necessary for different products.

As such, we question:

- How the default assumptions can be justified without referring to a financial product?
- How a member can easily relate the default assumptions and strategy to the products offered by a fund?
- Where a fund offers number of Growth investment options (for example a passively managed option and an actively managed option), surely it is important to inform the member on which product the assumptions have been determined.

We believe that referring to a specific financial product is not the same as advertising or promoting it.

We also expect most users of a calculator on a particular fund's website would be members of that fund. It is therefore important a calculator enables them to easily compare likely outcomes from the range of products offered by the fund.

Recommendation B1d

The updated Class Order should enable a generic calculator to reference a particular product (or at least reference a particular product as an example of the type of product for which the calculator could be used). For example, it should be allowed to use words such as "The assumptions adopted are considered reasonable for the XYZ Fund Australian Shares investment option."

B1Q2 Instead of remaking [CO 05/1122], should ASIC allow [CO 05/1122] to sunset on the basis that providers of generic financial calculators can refer users to the calculators provided on ASIC's consumer website, MoneySmart, for additional financial information and education?

No. The MoneySmart calculator should not be the only avenue of this nature that consumers have to consider additional financial information and education. Furthermore, we note that the MoneySmart calculator does not work seamlessly on many mobile devices (or indeed at all on some); the user interface is not engaging to consumers nor does it allow institutions to proactively differentiate themselves from their competitors in respect of providing financial insights to their customers. As such, we strongly oppose any sun setting of Class Order 05/1122.

Recommendation B2 ***The Class Order should not be allowed to sunset and superannuation funds should be able to provide appropriate financial information and education to their members.***

B1Q3 Do these proposals help achieve our objective of facilitating the provision of useful and accurate information about financial products and services through generic financial calculators?

Although there are some improvements, ultimately the proposals in our opinion do not go far enough to provide useful and accurate information to consumers. We would have expected to see greater flexibility (whilst maintaining the appropriate safeguards) from ASIC to drive innovation and customer engagement. An example is the prohibition of references to a particular product. This, in our opinion, reduces the viability of providing useful and accurate information to members and makes it more difficult for members to understand the calculator output. We would welcome the opportunity to consult further on how ASIC may continue to partner with industry to strive to provide more useful and accurate information to members.

Recommendation B3 ***More flexibility is necessary to appropriately engage members, particularly in the area of referencing particular products.***

B1Q4 Do you think the current requirement that a generic financial calculator must display to the user in the ordinary course of its use clear and prominent statements and explanations is achieving its objective of promoting user engagement with this information?

Effective consumer engagement is paramount. The current requirement when undertaken appropriately can assist consumers in an engaging way; however, allowing the layering of disclosure will better enable providers to design calculators which can be even more engaging for consumers than the current requirement.

Recommendation B4 ***Although allowing layering of disclosure will enhance the objective of promoting user engagement, additional flexibility should be incorporated to further enhance user engagement (e.g. the ability to reference a particular product).***

B1Q5 If we include a requirement that future projected amounts must be adjusted for inflation, should we prescribe an appropriate measure of inflation or should the provider be left to make assumptions about the rate of inflation? Would the Consumer Price Index averaged over a period of time, or the inflation assumptions used by ASIC's MoneySmart calculators, be an appropriate measure of inflation? Please give reasons for your view.

We support a requirement that future projected amounts be adjusted for inflation, at least for discounting periods of 2 years or more.

However, if inflation adjustments are not made where the discounting period is less than two years, this may confuse some members as well as making the program design more complex. Flexibility would be needed to enable providers to adjust for inflation for shorter periods as well.

The choice of deflator should be based on CPI or AWOTE.

In our view, the most appropriate deflator during the pre-retirement period would be based on AWOTE rather than CPI, as consumers are expecting their standard of living to increase (AWOTE is a measure of the combined effect of inflation and increased standard of living).

During the pension drawdown phase, CPI might be considered a more appropriate deflator as retirees are less likely to be expecting increases to their standard of living. We acknowledge that the use of different deflators for different periods may add some confusion.

In any case the deflator should NOT be based on past experience as this is not necessarily a good guide to the future. For example, past CPI figures may be artificially inflated (for example due to an increase in the GST) and future expectations may be significantly different to past experience (such as the CPI averaged over a period of time).

The deflator should be based on the best estimate of future experience. To ensure consistency this could be an estimate determined by ASIC or the Australian Government Actuary.

AWOTE is appropriate for projecting to retirement. After retirement, the provider should have the choice of using CPI or AWOTE, which could be altered by the user.

Recommendation B5

Future projected amounts should be adjusted to reflect current day values.

The adjustment should either be mandated for all periods or mandated for periods of 2 or more years (with flexibility to adjust for shorter periods).

The adjustment should be made in terms of a best estimate of future AWOTE increases during the pre-retirement phase.

More flexibility should be allowed in the draw down phase to allow deflators based on either AWOTE or CPI.

The Class Order should allow calculators to enable users to modify the deflator assumption.

B1Q6 Should we require that generic financial calculators include a field relating to fees and costs? Alternatively, should we allow the provider the flexibility to determine disclosure about fees and costs subject to the requirement that if the calculator does not include a provision for fees and costs this has to be clearly and prominently explained, including the impact of this limitation?

In order to provide an appropriate estimate of a future retirement benefit, calculators must allow for fees. Without a fee allowance, the retirement estimate may be significantly overstated. It would be preferable if these were allowed for explicitly rather than using a net of fees investment return as this explicit approach is likely to achieve a more appropriate estimate. As a minimum, allowance should be made for administration and investment management fees. Providers should be able to also take into account insurance premiums and other fees and costs where relevant so as to further enhance the consumer's understanding of the estimates provided by the calculator.

Disclosure is important and there should be requirements to clearly disclose the fees which have been assumed.

Recommendation B6

The Class Order should mandate allowance for administration and investment fees as part of the default assumptions with flexibility for providers to allow for other fees and costs. The default assumptions should be clearly described.

B1Q7 If ASIC required generic financial calculators to include a field relating to fees and costs, should we prescribe standardised fees and costs? On what basis should the fees and costs be calculated and what requirements should ASIC set?

We strongly argue against the introduction of any standard fees and costs being prescribed by ASIC as these have the potential to be misleading to consumers.

For example, standardized fees may lead to an artificially inflated or artificially constrained retirement estimate. For example, fees for a particular product may be significantly higher than fees for a different type of product, even within superannuation.

For example, the fees applicable to a superannuation investment option which concentrates on infrastructure investments are likely to be significantly higher than the fees generally applicable to a cash option.

Similarly, the fees to be incurred by a member with a small balance may be considerably different to the fees for a member with a large balance.

Therefore we believe any assumption concerning fees and costs should be set by the provider having regard to the product considerations relevant to the likely user group.

Recommendation B7

The Class Order should not mandate any standard assumption for fees. However it should require the default fee assumption to be determined by the provider and based on a reasonable estimate of the fees to be incurred by a user in the likely user group. The assumptions should be clearly disclosed. An estimate should be considered to be reasonable if it reasonably reflects the fees to be incurred by a member of a relevant product issued by the provider.

B1Q8 How has the requirement in [CO 05/1122] that the provider of a generic financial calculator must take reasonable steps to ensure that the calculator does not advertise or promote a specific financial product worked in practice?

The requirement not to advertise or promote a specific financial product in practice has caused major difficulties to providers and prevented them from innovating improved engagement and education channels with their customers. The restrictions resulting from this requirement are a major concern.

For example, we consider it reasonable that the names of the investment strategies listed in a particular calculator should reflect those available to the user (to make it easier for the user to understand). However, under the current Class Order, if those names are not generic enough (eg. Mercer Growth) they need to be modified for the calculator, which risks confusion for users and a poor member experience.

Another example is the lack of clarity as to whether ancillary marketing material (not specific to the calculator) that is positioned elsewhere on a fund website (e.g. a panel highlighting the benefits of rolling your super into the fund), can be included on the same screen as a calculator. The lack of clarity on this issue needs to be resolved. This is particularly important in a mobile first environment where “real estate” (the space on the mobile platform) is significantly limited.

Finally the Class Order is not clear whether ‘specific financial product’ means a class of financial product (e.g. account based pension) or a particular financial product (e.g. ‘Mercer’ Personal Super Division Account Based Pension).

Recommendation B8 ***Greater clarity is required as to the scope of these restrictions which should be made more flexible by allowing reference to particular products (at least as examples of the products for which the calculator/assumptions may be appropriate).***

B1Q9 Do you think that we should introduce a new express requirement that statutory assumptions, such as the taxation rates or the rates of compulsory superannuation contributions, must remain up to date?

Whilst it is important for calculators to remain up to date, it is unclear what is meant by “up to date” when many legislative changes may not have immediate impact but instead are either phased in over time or apply from a future date. It is particularly important that calculators include sufficient details of the statutory assumptions adopted.

Recommendation B9 ***A requirement should be introduced for calculators to show:*** ***1. A list of relevant legislative provisions (including legislated future changes) that have not been allowed for in the calculations; and*** ***2. The date(s) at which assumptions and existing parameters (eg taper rates and thresholds for age pension eligibility) were last updated or reviewed***

B1Q10 If the proposals about the 'super estimator' referred to in paragraph 9(d) are implemented, should ASIC make any changes to the relief in relation to superannuation funds retirement benefit projections where the super estimator applies?

As indicated in our submission to The Treasury on Improved Superannuation Transparency, we do not support the inclusion of a "super estimator" at this stage. We have included an extract from our submission in Appendix 2 setting out our reasons.

In particular, the results from the proposed super estimator are potentially misleading given the limited assumptions it utilises.

Furthermore, it is unnecessary in light of the more sophisticated generic calculators that are available in the market. We also note the super estimator does not comply with the current class order and it is our view that implementing a product of a lesser standard is not an appropriate solution.

Recommendation B10
The requirement to add a superannuation estimator to dashboards should be deferred until full and proper consideration can be given to the benefits and disadvantages.   ***However, if it becomes a requirement to include a superannuation estimator in Product Dashboards, this should not impact on the relief in relation to generic calculators. Providers should be encouraged to engage and educate customers with innovative and best practice advice solutions rather than being confined to a generic calculator that may not be appropriate for their customers***

B1Q11 Please give details of any additional costs associated with the implementation of our proposals. If possible, please quantify these costs.

> The answer to this question ultimately depends on the sophistication of the provider of the generic calculator. For an established provider with a sophisticated generic calculator the proposed changes would not be overly costly to providers. The exception to this statement is if the proposed reporting of likely breaches was implemented. This would require substantial increased soft costs which would have to be absorbed by the business ultimately at no benefit to members.

B1Q12 What benefits do you consider will result from these proposals? If possible, please quantify these benefits.

The benefits of these proposals are not particularly significant to consumers or industry. They do not assist industry in innovating and providing customers with useful insights into their financial circumstances. Being able to refer to particular products (without advertising or promoting them) would add far more value to customers in educating and engaging with their financial circumstances. Ultimately this will lead to better informed, engaged and empowered customers.

APPENDIX 2: Extract from Mercer submission to The Treasury in relation to "Improved Superannuation Transparency"

Superannuation estimator

We do **not** support the addition of a superannuation estimator to product dashboards at this time because the estimator appears designed for less financially literate consumers (where education is the primary goal) while the dashboards are designed for high level comparative purposes.

Such disclosure is inappropriate for the following reasons:

- Inappropriate decision making
    - Although we agree dashboards should be useful and should engage readers, the inclusion of a superannuation estimator, as proposed, is very dangerous. Decisions on choosing a fund based on the comparison of retirement estimates is totally inappropriate and trivialises superannuation. In particular, there is a risk that less financially literate users would interpret the estimates as being personally accurate and would not understand the limited purpose for which the estimator is intended (i.e. as a 'high level' sifting tool only).
    - The estimator will not use the actual fees that would be charged to a particular reader, making the estimator inappropriate for comparison purposes.
    - The estimator will apparently use the return target provided by each superannuation fund. This may result in RSE licences manipulating the outcomes by overinflating or stretching target returns, again highlighting that such estimators should not be used for comparison purposes.
    - Although not the intention, it is possible some readers will note the estimator is based on an ASIC engine/assumptions etc. and may consider, inappropriately, that it is reasonable to choose a fund based solely on the estimates shown on different dashboards. At the very least, wording should be included, in close proximity to the link, to the limitations of the estimator – namely that it will not provide a reliable personalised estimate.

- Lifecycle options
    - The draft requirement assumes the investment mix remains constant until retirement, which is unrealistic and misleading for lifecycle options. Allowance must be made for changes in investment allocation and fees as the reader moves through different age bands, or at least there should be an ability to warn readers that the estimator is not suitable for comparing products with lifecycle options.
- Disclosure requirements
    - As drafted, the estimator would not satisfy the requirements of ASIC CO 05/1122 for calculators on fund websites or the amendments to these requirements proposed by ASIC in its Consultation Paper 249. Although we understand that the estimator is intended for a different purpose to fund website calculators, it is not apparent why different disclosure requirements should apply.
- Inconsistency with FSI recommendations
    - The estimator's output of a lump sum benefit at age 65 is inconsistent with the recommendation of the Financial System Inquiry to show projected benefits in income form.
- Eligibility for age pension
    - The use of age 65 for the estimator's output is inconsistent with the eligibility age for the age pension, which will be 67 for most potential readers.
- Only part of a portfolio
    - For Choice dashboards, the estimators would assume 100% of the reader's retirement savings are invested in the choice option. This is highly unlikely where the option only invests in one asset class. Again, there should at least be a warning for this purpose.
- Confusion
    - It is likely the estimator will show different outcomes than the results produced by any other calculator provided on the fund's website or even ASIC's MoneySmart

calculator. Members (particularly those less financially literate) will be confused and potentially critical.

- Pressure on RSE licensees to maximise outcomes
    - Where estimators are used for comparison purposes, the outcomes may lead to:
        - reductions in service levels in an attempt to minimise fees; and/or
        - reductions in investment performance by minimising investment costs, including moving away from performance fees and moving to index based products rather than active management.

Recommendation 2.12

The requirement to add a superannuation estimator to dashboards should be deferred until full and proper consideration can be given to the benefits and disadvantages.