



12 April 2019

Kathy Neilson
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Australian Securities and Investments Commission
Level 5, 100 Market Street
Sydney, NSW 2000

email: feeandcostdisclosure@asic.gov.au

Dear Kathy,

Consultation Paper 308

Review of RG97 Disclosing fees and costs in PDSs and periodic statements

The Actuaries Institute is pleased to make this submission in response to Consultation Paper 308.

We are supportive of CP 308 and believe CP 308 represents a meaningful step forward in dealing with the complex issues of disclosing fees and costs.

We support most of the proposals of CP 308. For the handful of areas where we believe some further modifications would assist consumers, we have provided our feedback in response to the corresponding questions asked in CP 308 in the attachment to this submission paper.

Should you wish to discuss any aspects of this submission or require any further information please contact either Tim Jenkins, Convenor of Superannuation Practice Committee (phone 0414 887 137 or tim.jenkins@ricewarner.com) or Elayne Grace, CEO of the Actuaries Institute (phone 02 9239 6100 or elayne.grace@actuaries.asn.au).

Yours sincerely

A handwritten signature in black ink, appearing to read "N. Rubinsztein".

Nicolette Rubinsztein
President



Attachment to Submission to Consultation Paper 308

Introduction

The Actuaries Institute is pleased to make this submission in response to Consultation Paper 308. For your convenience, the body of this submission follows the question order of CP 308, with reference to the two Attachments to CP 308. Our key recommendations are highlighted in bold.

The views in this submission draw on our 2018 Indirect Costs Survey, which was completed by 49 superannuation actuaries and members of ASFA and was emailed to yourself on 18 February 2019. The survey focuses on superannuation products, but we believe most of the suggestions are also relevant for collective ("managed") investment products.

B1Q1 - Changing the superannuation product 'Fees and costs template'

We support proposal B1(a) on changing the superannuation product 'Fees and costs template', namely the intention to introduce requirements to:

- (i) present all administration fees and costs as one-line item, by merging administration fees and indirect costs that relate to administration or operation of the superannuation entity;
- (ii) present all investment fees and costs as one-line item, by merging investment fees and indirect costs that relate to investment of the superannuation entity's assets;
- (iii) remove advice fees (intra-fund advice costs) as a line item, and include this cost in the disclosure of administration fees; and
- (iv) group together the 'Ongoing annual fees and costs' separately from the 'Member activity related fees and costs'.

These are proposals (except perhaps for the proposed components of (iv) above) that the Institute has been advocating for many years.

Proposal B1(v) refers to changes to the 'Example of annual fees and costs' which are illustrated in Figure 3 of the Draft Updated RG 97 (Attachment 1 to CP 308). Figure 3 includes the sentence "You should use this table to compare this superannuation product with other superannuation products."

For the following two reasons we recommend caution with use of this sentence and with the proposed layout of the 'Example of annual fees and costs':

- 1 For the majority of members whose account balance is not approximately \$50,000 the table can potentially provide misleading information about product costs and by following it they could potentially choose products that are less suitable to their needs.
- 2 As explained in our comments regarding to B5Q1 below, we believe that product costs should not include transaction costs in the manner proposed. Transaction costs should instead be explained to consumers, as suggested in D5 of CP 308, within the context of information about returns.



If the sentence referred to above remains, we suggest that the 'Example of annual fees and costs' should be changed to show fees and costs for more than one account balance and to either:

- (a) exclude transaction costs and move them to 'Fees and Costs Details' (our preferred alternative), or
- (b) to qualify transaction costs to rectify 2 above (an example of this alternative is set out below).

We also believe that the 'Example of annual fees and costs' and the 'Cost of product information' should be made consistent with the layout of Product Dashboards. This would help consumers identify this key information in the relevant plan documentation.

We provided submissions to Treasury (12 April 2018) and to ASIC (19 December 2017)¹ with recommendations on Product Dashboards. The following is an example, based on "PRODUCT A" detailed in the Treasury submission, which illustrates one possibility of how to simplify the 'Example of annual fees and costs' based on alternative (b) above.

Example of annual fees and costs

This table gives an example of how the ongoing annual fees and costs for the *[insert name of generic MySuper product or other investment option as required by subclause 220(1)]* for this superannuation product can affect your superannuation investment over a 1-year period. You should use this table to compare this superannuation product with other superannuation products.

EXAMPLE – Balanced Investment Option	\$10,000 account balance	\$50,000 account balance	\$250,000 account balance
Investment fees and costs	\$57	\$285	\$1,425
Administration fees and costs	\$20	\$100	\$500
Cost of product	\$77	\$385	\$1,925

The table above excludes transaction costs because reported investment returns for all superannuation products already allow for transaction costs. Transaction costs can vary significantly for different investment strategies. Low transaction costs may be a result of passive indexed investment styles and high transaction costs may be a result of active investment styles.

Transaction costs (net)	\$15	\$75	\$375
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¹The Actuaries Institute's submission to The Treasury re MySuper and Choice Dashboards on 12 April 2018 (page 1 – 5) and attached submission to ASIC re Proposed MySuper Product Dashboard on 19 December 2017 (page 6 – 10), <https://www.actuaries.asn.au/Library/Submissions/FinancialServicesReform/2018/20180412SubTreasMySuper.pdf>



B3Q1 - Including 'Cost of product information'

The proposed 'Cost of product information' is based on a \$50,000 account balance. **We recommend considering more than one account balance** to cover members in a range of different situations. For the reasons explained in Appendix A to this submission we recommend specifying three account balances (\$10,000, \$50,000 and \$250,000).

We also recommend that the 'Cost of product information' for each investment option should use the same layout as for the 'Example of annual fees and costs' and Product dashboards.

B3Q3 - Including 'Cost of product information'

It is proposed that the 'Cost of product' information incorporate a contribution of \$5,000 on the last day of the year. This is appropriate for those very few products which base administration fees or costs on contributions. Nowadays, very few if any plans base fees and costs on contributions. Thus, for the vast majority of products it is irrelevant and, for these products, we recommend that this requirement be omitted. The same should also apply to the 'Example of annual fees and costs'. We believe that this change would simplify the disclosure and assist both consumers and providers.

B4Q1 - Simplifying periodic statements

It is proposed that periodic statements contain the following three lines:

- (i) 'Fees deducted from your account';
- (ii) 'Fees and costs deducted from your investment'; and
- (iii) 'Total fees and costs you paid'

It is extremely difficult to understand the (often subtle) differences between these three amounts and to decide which ones are relevant. To avoid confusion, **we recommend that either line (ii) be omitted entirely or that it be changed to a requirement to separately disclose and name insurance fees, switching fees and any other "activity-related" fees** and to reposition this information separately from:

- (i) 'Administration and investment fees deducted from your account'; and
- (ii) 'Administration and investment fees and costs you paid'.

B5Q1 - Changing the treatment of transactional and operational costs

Items B5 (b) proposes to include explicit transaction costs and counterparty spreads in the calculation of the 'Cost of product information'. We agree with this proposal but the way it is to be implemented needs considerable change – suggestions about how this might be done are included in our comments on B1Q1.

Paragraph 85 (page 31 of CP308) in the Rationale section explains, that REP 581 notes that *"on balance, perhaps the preferred direction is that unless or until it can be shown through consumer testing that transaction costs are in most cases not relevant to the decision being made, and there are no material concerns about possible gaming, transaction costs as disclosed in the 'Fees and costs template' should also be included in the 'Example of annual fees and costs' and the 'Cost of product information'."*



We believe that the quantum of transaction costs should not be included in 'Cost of product' information. For an active fund manager, the annual dollar transaction costs could fluctuate a lot and this is likely to distort the 'Cost of product' information if included within that item. More importantly, there are two aspects of this issue which it is most unlikely will be shown through consumer testing.

The first, as contained in our 7 August 2017 letter to Treasury², is that **transaction costs should be shown separately from other fees and costs. Their nature is entirely different to other fees and costs** – for example, their impact is reflected in gross investment performance. Other fees and costs are reflected in net investment performance. Also, a significant part of transaction costs relates to situations involving switches of securities where the switch is only made because the investment manager believes that the new securities will outperform the old securities even allowing for the transaction costs. Thus, in these situations, the transaction costs would not be expected to reduce investor returns (relative to not undertaking the transaction).

The second is that we believe transaction costs should be explained to consumers, as suggested in D5 of CP 308, within the context of information about returns. But certainly, we believe they should not be included in the 'Cost of product'. Further suggestions and explanations about this are included in our comments B1Q1.

B10Q3 – Disclosing performance fees

Paragraph 108 (page 40 of CP308) in the Rationale section states *"We propose to amend cl 209(b)(iii) of Sch 10 to require disclosure of the five-year average for each relevant performance fee that makes up the total performance fees. We do not propose to require disclosure of the individual annual performance fees that make up the five-year average. We believe this would require the issuer to provide too much information, which may be confusing for consumers and could reduce the practicability of the fees and costs disclosure requirements for industry."*

We have previously recommended that the individual annual performance fees for each of the last three years should be disclosed. We have no problems with your proposal to use a five-year average but we suggest that the industry should be encouraged (but, initially at least, not required) to also disclose the individual annual performance fees for each of the last five years where trustees believe this is practical and will assist consumers.

B11Q2 - Clarifying the treatment of costs paid out of reserves

If a fund maintains administration reserves, where the fees levied on members' accounts (or the costs deducted from crediting rates or unit prices) are transferred into such reserves, then we suggest that the fees and costs transferred to those reserves, as well as any tax benefits related to fund expenses that are transferred to the administration reserve, be included in the disclosed fees and costs. When amounts are transferred out of such reserves to meet expenses, these should not be treated as an ongoing fees or costs. An exception might apply in the unlikely event that administration reserves were negative.

² The Actuaries Institute's letter to Treasury re Product Dashboards and Disclosure, <https://www.actuaries.asn.au/Library/Submissions/Superannuation/2017/2017807TreasuryDashboardsASIC19AprilMeetingFnI.pdf>.



For the reasons explained in our submission to ASIC on 22 October 2018³ we suggest that amounts transferred into other reserves (i.e. other than administration reserves) should not be treated as ongoing fees or costs. Instead, we recommend that transfers to and from such reserves should be disclosed in accordance with the requirements of sub-regulations 7.9.37 (k), (l) and (m) of the Corporation Regulations, separate from ongoing fees and costs.

C1Q1 - Consumer testing some proposed changes

We are concerned that the proposal C1(b) seems to suggest that administration fees and costs should be merged with investment fees and costs. We believe that such “merging” would be a very backward step. This is because in order to give members and prospective members a sound basis for comparing the costs of two or more superannuation funds, the members need to know and consider:

- (1) The fund administration fees and costs and the services provided for those fees and costs, and
- (2) The investment fees and costs and the expected net investment returns in respect of all the various investment options.

Administration fees and costs and investment fees and costs have different attributes which make it necessary to demonstrate their effect on members in different ways. Having separate figures for administration and investment costs is not only appropriate for comparison purposes but also makes it easier to select a fund providing the administration services required and the desired range of investment options.

If this key aspect of the CP 308 proposals is to be decided primarily on the basis of consumer testing, then we suggest that participants in the program would need to be given very carefully prepared information about the respective attributes of investment and administration services, fees and costs. Perhaps they should also be asked, if purchasing two apples and three oranges, would they prefer to know merely the cost of five fruit, or would they prefer to know the separate costs of apples and oranges? (This is based on the analogy we used to explain the reason for separating fees and costs into investment and non-investment components in our submission to Super System Review on 18 November 2009.⁴)

C6Q2 - Clarifying in RG 97 the treatment of amounts paid by third parties or offset against other amounts

Paragraph 130 (page 49 of CP308) in the Rationale section states “We believe that the fact that a fee or cost is paid for by a third party does not affect its characterisation as a fee or cost for disclosure purposes. Including these amounts ensures that the true costs associated with the product or option are disclosed to consumers.” Though we generally agree with this, **we recommend that an exception should apply to the situation when an Employer decides to pay extra contributions to cover all fees and costs, or all administration fees and costs.** The main reasons for suggesting this exception is that the situation is beneficial to the consumer and that such an exception would be consistent the proposals for Defined Benefit members.

³ The Actuaries Institute’s submission to ASIC re Outstanding Superannuation Matters on 22 October 2018, <https://www.actuaries.asn.au/Library/Submissions/Superannuation/2018/20181022LetteASICreOutstandingSuperannuationMattersFnI.pdf>

⁴ The Actuaries Institute’s submission to Super System Review on 18 November 2009, https://www.actuaries.asn.au/Library/2009_1119_IAAust_Sub_Super_System_Review_Phase2_Final.pdf



D5Q2 - Explaining transactional and operational costs to consumers within the context of information about returns

We believe that explaining transaction costs within the context of information about returns would help consumers compare products and make informed value for money decisions – see our comments regarding B5Q1.



Attachment 1 to CP 308 - Draft Updated RG 97

Consumer advisory warning

We note that the current and draft updated RG 97 both contain a 'Consumer advisory warning' which commences:

DID YOU KNOW?

Small differences in both investment performance and fees and costs can have a substantial impact on your long term returns.

For example, total annual fees and costs of 2% of your account balance rather than 1% could reduce your final return by up to 20% over a 30 year period (for example reduce it from \$100 000 to \$80 000).

We draw to your attention that in the second paragraph of this extract, the word "return" is confusing and possibly incorrect. We believe that a far more appropriate word would be "benefit". Most consumers would interpret "returns" and "return" as investment returns not benefit returns.

Other comments on the Draft Updated RG 97

1. We suggest RG 97.126 be expanded to also refer to situations when tax deductions are not passed on to an accumulation member. Consumers should be advised about this and have the impact quantified if possible.
2. We suggest RG 97.281 should also refer to indirect administration costs.
3. We suggest RG 97.334 should clearly differentiate between "trustee-imposed buy-sell spreads" and "investment manager-imposed buy-sell spreads" because the disclosure requirements of each are very different.

Attachment 2 to CP 308 – Draft Amendment to Schedule 10

We suggest the references to performance fees in Page 27 of the draft amendment to Schedule 10 be explicitly specified to be expressed as percentages of option assets (not as dollar amounts)