Consultation Paper 351: Superannuation forecasts: Update to relief and guidance

Submission

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David Bell

About The Conexus Institute

The Conexus Institute is an independent, not-for-profit research institution focused on improving retirement outcomes for Australian consumers. Philanthropically funded, The Institute is supported by the insights of a high-quality advisory board, whereby each member's involvement is on a pro-bono basis. The Institute adopts a research-for-impact model and frequently collaborates with researchers from academia, associations, and industry. Research is generally made open source to create transparency and accountability. The Conexus Institute exists with no commercial relationships. Further information here.

About David Bell

Dr David Bell is Executive Director of The Conexus Institute. Bell's career has been dedicated to the investment and retirement sector. He has worked with both commercial and profit-for-member firms, and ran his own consulting firm. Bell worked with APRA in the development of the APRA Heatmap. Academically, Bell taught for 12 years at Macquarie University and in 2020 completed his PhD at UNSW which focused on retirement investment problems. Full bio here.

***** The author is willing and able to participate in further consultation. *****

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1. Summary

Well done to the team at ASIC for progressing class order relief around retirement estimates and superannuation calculators. Many positives have been detailed in the consultation paper, with the highlights being:

- Integrating retirement estimates and superannuation calculators into the same policy framework.
- Adopting a principles-based approach, resulting in greater flexibility for users of the class action.

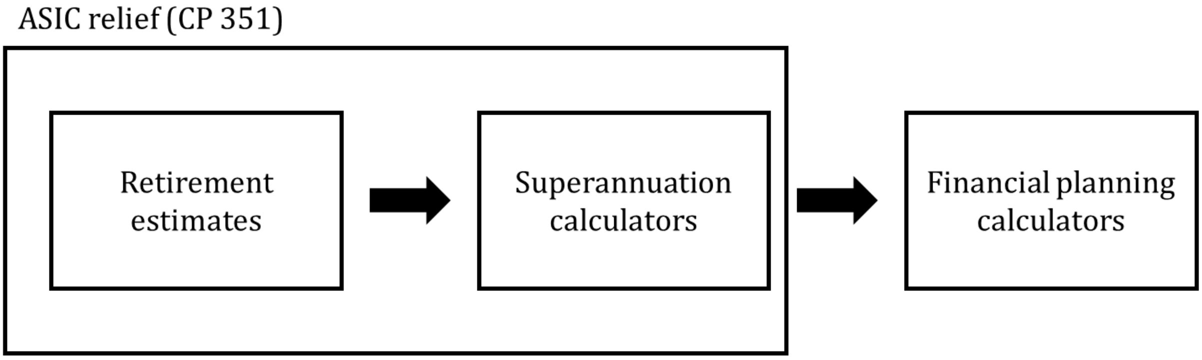
We respond to a selection of questions from the consultation paper and make a small number of suggestions.

We anticipate that funds will rely strongly on superannuation calculators in the foreseeable future. In this context, this work may serve as an important mechanism for implementing retirement income policy.

Accordingly, our suggestions account for how we envisage the role of retirement estimates and superannuation calculators evolving in the future. Some framing, technical and digital enhancements could contribute to greater adoption by funds and a more appropriate monitoring structure to complement a principles-based environment.

2. Positioning

Our basic interpretation of the consultation topic is reflected in the diagram below.



It is important to reflect on current retirement income policy settings. In our view present retirement income policy settings will fail to deliver significantly improved outcomes to consumers. The primary reason is the absence of an industry-friendly matching mechanism for super funds to match members to appropriate retirement solutions (broadly a mix of products and a drawdown schedule).

While it is not the purpose of ASIC's work on superannuation forecasts to solve this larger challenge, our recommendations are cognisant of the role that superannuation forecasts can perform in improving retirement income policy.

3.Suggestions

3.1. Re-name “Retirement Estimate” to “Basic Retirement Estimate

Static retirement estimates are very basic pieces of information. Arguably their engagement value exceeds the value of any insight that they provide. There is an uncertain benefit, and clearly risks, in consumers relying heavily on this information.

Re-naming “Retirement Estimate” to “Basic Retirement Estimate” reduces risk and may be a nudge to engage further (e.g. “I don’t just want the basic information, I’m curious to know more”).

3.2. Higher standards for superannuation calculators

We advocate that superannuation calculators need to meet higher criteria-based hurdles before they be permitted to incorporate certain features. We propose two stage gates:

1. Calculators must be interactive around all relevant assumptions before the Age Pension can be incorporated.

2. Calculators must present the range of outcomes (not just expected outcome) before multiple retirement products can be incorporated into the calculator.

3.3. Create tech-based functionality for ASIC moneysmart to be used by super funds

While there are examples of super funds which provide retirement estimates and access to superannuation calculators, there continue to be funds which do not provide these services.

In our view ASIC should do everything possible to facilitate universal provision of retirement estimates and superannuation calculators by super funds. There is an opportunity for ASIC and APRA collaboration on this issue, whereby universal provision would be a healthy informal collaborative objective. Here, ASIC would facilitate access and APRA promote adoption through its focus on retirement outcomes, member outcomes and ongoing engagement activities.

Specifically, ASIC could:

- Enhance the ASIC moneysmart retirement calculator to align with standards detailed in this submission (namely the ability to present the range of outcomes).

- Develop the technology to enable web-based access to the moneysmart retirement calculator (e.g. through scanning a QR code) which uploads the member assumptions (used in generating the retirement estimate) into the moneysmart retirement calculator to ensure no change in initial projection.

APRA could:

- On an if-not-why-not basis enquire why funds which aren't providing access to retirement calculators, especially if the moneysmart retirement calculator is available on an open-source basis.

3.4. Online template for assumptions and justification

We advocate for the development of an online template which acts as a record of process leading to the development of important assumptions on investment returns and fees. This would also capture other point-in-time data such as investment objectives.

We thank Super Consumer's Australia for sharing this idea with us.

We envisage this would have multiple benefits:

- Formalises minimum standards to appropriately complement a principles-based approach.

- Creates a cross-sectional dataset that may be of value to ASIC for future research.

3.5. Additional disclaimers to members

We propose the additional disclaimers are included:

1. That a member may be entitled to the age pension and refer the member to a link that can assist (preferable the fund's superannuation calculator).

2. That it is not appropriate to compare this retirement estimate with a retirement estimate from any other source (as the assumptions may be different).

3.6. Privacy around any submitted information

Clarity should be provided (if it hasn't already) around the ownership, treatment and management of data inputted into interactive calculators by members. We don't make any specific recommendations on this topic.

4. Specific questions and issues

We only address questions where we think our insights are of value to ASIC.

B3Q1 Do you agree with our proposal for principles-based disclosure requirements? Why or why not? Should there be any conditions or other steps taken to address particular risks arising from a principles-based approach?

We support a principles-based approach. It allows funds a more appropriate degree of flexibility to provide superannuation and retirement projections to their members.

B6 We propose to allow trustees to deliver retirement estimates through member online portals, as well as through periodic statements. We will amend our guidance to clarify that retirement estimates can be provided to members more frequently than through periodic statements. We will also clarify in our guidance that a retirement estimate may be given in video or audio format provided the requirements of our relief are met (e.g. in relation to disclosure).

In our view this all makes good sense.

C2Q1 Do you support trustees and other providers having flexibility to set their own reasonable assumptions for investment earnings, fees and costs, including on the basis of the product a member is invested in? Why or why not?

We consider it appropriate for trustees and other providers to have this flexibility. However, we think it is important that this process is well-governed, and that trustees and other providers be required to document the basis on which assumptions are made. We recommend that ASIC develop an online template which must be completed (see 3.4).

C2Q2 What are the risks to members and to industry of trustees setting their own reasonable assumptions for investment earnings, fees and costs relating to the product in which a member is invested in, or a product which the trustee offers? How can these risks be mitigated?

The risks are agency-based and governance. The primary agency-based issue is promotion. We assess this risk as low. Governance issues could be managed through formalised governance of the assumption setting process. We recommend a template-based approach (see 3.4) to establish a minimum governance standard that ASIC can monitor.

C2Q3 Should trustees have greater flexibility to set other types of assumptions, either for a retirement estimate or superannuation calculator? Why or why not?

In our view the consultation paper details an appropriate amount of flexibility. No further flexibility is required to provide a basic retirement estimate which may engage members to seek a more informed estimate.

C5Q1 Should trustees be expected to set the same assumptions across all superannuation calculators and retirement estimates they provide? In what circumstances should assumptions be able to differ?

We can see no reason why differences are necessary (under like-for-like situations).

C6Q3 In working out a retirement estimate, would it be practical for trustee to set assumptions about investment earnings, fees and costs that may differ based on the products members are invested in? Why or why not? Are there alternative approaches?

We believe it is appropriate and practical for trustees to set product-specific assumptions. All investment assumptions would reference investment objectives while the trustee has good insight into long-term product administration expenses. Both these issues are discussed in more detail in C6Q4.

C6Q4 What guidance should ASIC provide on how assumptions about investment earnings, fees and costs should be set? Would it be appropriate for trustees to set assumptions on the basis of existing investment return objectives for superannuation products they offer (e.g. the return objective disclosed in the Product Disclosure Statement (PDS) or set by the trustee board?)

Assumptions need to link investment objectives and PDS disclosures, but there are reasons why differences may exist.

For investment earnings there exists a technical issue:

- Our understanding is that in determining investment objectives, a trustee needs to have an appropriate degree of confidence of the objective being achieved. Our understanding of industry practice is that this is generally a likelihood threshold level greater than 50% (e.g. it might be 65%). By comparison the basis of inflation and wage expectations are mid-point estimates, which broadly aligns with a 50% expectation. If a trustee were to determine investment expectations on a similar basis, they would generally be higher than stated investment objectives.

For fees and costs, fund behaviour in the short-term may not align with long-term expectations:

- Post the Your Future, Your Super performance test has resulted in some short-term fee decisions (e.g. one fund has announced zero admin fees).

- Trustees may have insight into long-term assumptions for fees which would form a better estimate.

Given these issues, we suggest that:

1. On investment returns, ASIC provides guidance that a likelihood-based adjustment is not required (i.e. investment objectives are appropriate inputs). This would result in the retirement estimate erring on the side of conservatism, but not dramatically so.

2. Trustees be required to develop long-term forecasts for fees and costs.

3. The process of determining assumptions creation be recorded using the template-based approach detailed in (3.4).

C7Q1 Would requiring trustees to make reasonable assumptions about administration fees based on the administration fees paid by the member over the previous year be workable in practice?

We have some concerns with this approach. These are detailed in our response to C6Q4.

C7Q3 Should we allow or require trustees to set different default assumptions for administration fees in the accumulation and retirement phases when working out a retirement estimate? Why or why not?

Trustees have the discretion to charge different administration fees across their product range. There are examples in practice of significant differences in administration fees between the accumulation and retirement options of a super fund. There can be rational reasons for this including the management of member cross-subsidisation.

In this context it is appropriate to allow a trustee to set different default administration fee assumptions.

However, given our responses to C6Q4, the trustee has the important role to develop long-term fee expectations, which may differ from present fees.

Separately, we note the different tax settings for accumulation and decumulation. All else equal, this creates a differential in investment return expectations between accumulation and retirement products.

C8Q1 What are the advantages and disadvantages of prescribing a default retirement age and drawdown period for superannuation calculators and retirement estimates under our relief?

Our view is that retirement estimates are basic estimates with known limitations. Their benefit lies as much in framing and engagement as much as the information itself. In this context we consider a default retirement age to be a reasonable approach.

Re-framing retirement estimates as a "Basic Retirement Estimate" (detailed further in this submission) may further reduce the disadvantages of default assumptions in general.

C9Q1 How do superannuation calculators show forecasts representing different types of retirement income products (such as account-based pensions and annuities) under ASIC's current relief? How could ASIC's proposed relief facilitate calculators for different types of retirement income product in a way that does not advertise or promote specific financial products?

We only address the second part of this question.

Different retirement products create varying retirement outcome profiles. In this context, profile extends beyond expected outcomes and considers the distribution of possible retirement outcomes (distribution captures the range of possible scenarios and the likelihood of different scenarios occurring. We note this is something that moneysmart does not do at present; it provides expected outcomes). Without providing such insight (rendering them risk-agnostic) retirement calculators inadvertently direct consumers to products which deliver the highest expected outcomes.

We suggest two possible paths that ASIC could take to address this issue:

1. Support the provision of simple (expectations-based) calculators and do not facilitate different retirement products.

2. Require calculators which compare products to provide a more detailed representation of retirement outcomes (namely the range of possible outcomes).

A third route would be to allow simple calculators to consider different retirement products but be accompanied by standard disclaimers that a consumer needs to consider further issues such as the range of outcomes to fully understand the features of the product. We don't consider this a great outcome – where would a consumer go to get this information?

This is a difficult issue. Given current retirement income policy and the challenges around provision of retirement advice and guidance by super funds, option (2) would provide a mechanism for providing their members with a mechanism to assess. However it would require ASIC to develop additional guidance.

C10Q1 For retirement estimates, what additional assumptions would need to be made to work out the annual income stream in the way that we propose? Should ASIC prescribe a specific formula? Why or why not?

We think it is not necessary for ASIC to provide a specific formula.

However, for the basic retirement estimate which does not include the age pension, it may make sense to provide the existing formula. A trustee could then detail (in the assumptions template) why they adopted the formula or otherwise the changes made (with associated reasoning).

When the retirement income profile is variable (due to minimum drawdown rules) we think it is important that a fund can present a diagram and quote the average retirement income through time (i.e. a single number).

C11Q1 What are the advantages and disadvantages of allowing trustees to include age pension amounts in a retirement estimate only if it is an interactive retirement estimate that allow the member to make changes to the assumptions?

There are many factors which impact age pension eligibility and entitlements. The existing assumptions which underpin basic retirement estimates create the risk of sizable inaccuracies. Hence, we agree with the logic of ASIC's proposal to not include the age pension in basic retirement income estimates. We recommend extra specific disclosure that relating to potential eligibility, along with a link to a calculator.

We note concerns raised by other groups that this may create anxiety and create an urge to over-save out of existing consumption. This can be investigated through survey work.

C11Q2 Should age pension amounts be required by default in interactive retirement estimates or in superannuation calculators? Why or why not?

We believe good practice is to include age pension in interactive retirement estimates. This would provide more valuable information for consumers. The opportunity for members to input their assumptions allows for a more appropriate determination of age pension eligibility and entitlements.

We do not believe that funds should be able to facilitate the consideration of different retirement products unless the age pension is incorporated into the retirement estimate. Exploring different retirement products necessitates a more detailed representation of retirement outcomes. This includes both consideration of age pension, and presentation of the range of possible outcomes (see C9Q1). We make a recommendation around both these issues (age pension presentation and presenting range of outcomes) in (3.2).

C15Q1 How should ASIC set values for the default inflation rates, and how frequently should these rates be reviewed?

The approach used by ASIC is reasonable. Generally it is difficult to obtain long-term forecasts. For instance the bank economist community rarely forecasts beyond three years.

ASIC could build in the ability to review forecasts and include them into a separate reference site rather than into the regulatory guide. Super funds would then be required to refer to the reference site for any updates.

This would provide ASIC flexibility to a develop a review mechanism. This could include any advisory committees that ASIC currently has in place.