AIA Australia Limited
(ABN 79 004 837 861 AFSL 230043)

PO Box 6111
Melbourne VIC 3004
Phone : 1800 333 613
Fax : 1800 832 266

AIA.COM.AU

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Nicole Chew, Senior Lawyer, Superannuation
Australian Securities and Investments Commission
GPO Box 9827
Brisbane QLD 4001
email: SuperForecastsConsultation@asic.gov.au

Dear Ms Chew

CONSULTATION PAPER 351 – SUPERANNUATION FORECASTS: UPDATE TO RELIEF AND GUIDANCE

Thank you for the opportunity to provide feedback on Consultation Paper 351. AIA Australia operates a Savings & Investments business that provides both superannuation and retirement income products, and we welcome the proposal to amend the current regulatory guidance on superannuation forecasts. We believe that fund members should be empowered to make decisions about how their superannuation balance can best support them in retirement, and effective retirement estimates and superannuation calculators are an essential input for this.

Relief and guidance that provide greater direction for trustees will allow them to better support members to make optimal decisions, including giving them greater comfort about drawing down their funds. These will also assist trustees to meet the increased obligations under the Retirement Income Convent (RIC). This is expected to help members achieve and balance a number of objectives, particularly maximising their retirement income and managing expected risks to sustainability and stability.

We support a principles-based assumptions approach, using standard inflation measures and bringing super calculators and retirement estimates together. The flexibility proposed to deliver these forecasts via online portals and statement messaging will ensure greater reach and usage. Interactive retirement estimates will likely drive greater engagement, and trustees should be positively encouraged to develop this capability.

However, we believe the proposed relief and guidance misses an opportunity to address two significant areas:

- Comparison between different income stream combinations
- Outputs should be modelled on a range of outcomes based on the selected product construct, rather than one which assumes a uniform rate of return each year in retirement, unless the intention is to allocate 100% towards a guaranteed income stream.

Superannuation forecasts should present a comparison between different income stream combinations

The RIC is expected to drive greater innovation in retirement income products; in particular, more options to protect against key risks such as inflation, sequencing and longevity.

Trustees are required to develop their retirement income strategies to assist members to achieve and balance three objectives – maximising their retirement income, managing expected risks to the sustainability and stability of their expected retirement income and having flexible access to funds during retirement

The relief and the proposed guidance should support these objectives and facilitate members making more informed decisions about their retirement income needs, with the option to seek personal financial advice in more complex scenarios.

It is not clear how the proposed guidance will support the development of tools that meet these objectives. Rather, the proposed guidance seems weighted towards a continuation of current practice – that is projecting

retirement income based on investing in an Account Based Pension (ABP) and any Age Pension entitlements (if included). Paragraph 95 of the consultation paper reinforces this:

"Our proposals are consistent with the member starting an account-based pension on reaching the retirement age. Account-based pensions generally offer flexibility (e.g., to withdraw capital or switch to a different product) and do not come with the cost needed to support a financial guarantee."

As drafted, this is likely to lead to tools that fail to consider critical inputs such as a member's risk profile or the desire for certainty over future income. If trustees are expected to properly engage members and provide increase in confidence during the draw-down phase, then the tools that support members making decisions about how they invest in retirement should be built to compare and contrast outcomes.

Both retirement estimates and superannuation calculators should allow and encourage members to compare different income stream combinations, by showing that there will be a trade-off between certainty achieved via guaranteed income streams versus the inevitable volatility (i.e. material range of outcomes) if only an ABP is selected. By allowing members to compare outcomes between different options for their retirement balance (where relevant, aligned to the strategy developed by that trustee for that particular cohort), including for example lifetime or deferred annuities, we expect member engagement to significantly increase, as they are empowered to determine the best approach to structuring their own retirement income needs.

While it will be important to balance the provision of additional or more targeted information against the risk of introducing extra complexity, we believe that superannuation calculators and interactive retirement estimates should include a simple risk profile – in particular, the user's preference for achieving a known (guaranteed) income in retirement. While most members' risk profiles would not be known when developing a retirement estimate, this could be presented as several scenarios reflecting different approaches to structuring retirement income; e.g., one which includes a guaranteed income component and one that does not. The scenarios presented in these retirement estimates would be aligned to the retirement strategy determined by the trustee for a particular member cohort. Failing to include these in retirement estimates and superannuation calculators is likely to create a false sense of security if a potential range of outcomes is not considered.

Outputs should show a range of outcomes

ASIC provided an update to the FSC and its members in December 2021, noting its intent to provide flexibility to providers on how outputs are presented, specifically noting the use of stochastic (or 'range of outcomes') modelling. This isn't particularly clear in guidance and isn't widely used by providers today. With the development of new innovative income stream products and a focus on managing sustainability and suitability risks, this is an important consideration for members in making optimal decisions.

A straight-line average investment return to life expectancy, consistent with the majority of forecasts used today, does not cater for volatility in how the averages are achieved. The timing and amount of volatility in investment earnings relative to drawdown patterns can lead to vastly different outcomes for members.

Additionally, using standard population mortality tables to estimate life expectancy means it underestimates a member's lifetime, on average, about half of the time. Further complicating this is the proposal to use default retirement age and period in retirement, that doesn't consider the differences between males and females.

Retirement estimates should take a more prudent approach and model a range of outcomes up to the maximum probable lifespan; for example, where there is a 10% chance of living beyond an age, rather than just an average life expectancy. For example, a female aged 65 has a 50% chance of living beyond age 89 years and a 10% chance of living beyond age 97 years, so a retirement model should model outcomes up to at least 97 years.[1]

Rather than displaying one scenario, based on straight line average investment returns (which are highly improbable), stochastic modelling or other 'range of outcome' modelling that presents a range of outcomes and the probability the individual income needs would be met, should be best practice.

This is likely to provide greater certainty to members to draw down capital and achieve a better lifestyle in retirement, as the risk of outliving their retirement assets has been effectively managed.

[1] Based on ABS Life Tables 2018-20.

We recommend the development of any superannuation forecasts should be based on stochastic modelling (or other 'range of outcome' modelling) for a range of scenarios and should be modelled up to maximum probable lifespan. This will assist members to understand their needs and assess the relative sustainability and stability of their retirement income and maximise their income over their retirement period.

SUMMARY OF RECOMMENDATIONS

Superannuation forecasts should present a comparison between different income stream combinations

Guidance should make it clear that best practice is to model a range of outcomes to improve consumer decision making and to reduce any mismatch of expectations in the future.

Where a range of outcomes isn't presented to consumers, the forecasts should include a clear disclaimer that the output is unlikely and may be impacted by factors like investment volatility and life expectancy.

Retirement estimates should be allowed to use specific financial product assumptions where a guaranteed income stream product is used, as the assumptions are highly customised and specific to the product issuer and the member's characteristics (age, gender, reversionary status and level of death benefit).

In addition to our key points above, we have provided responses to some of the proposals in the consultation paper in the Appendix.

Should you wish to discuss any aspects of our response please contact [redacted] in the first instance on [redacted]

Yours sincerely

[redacted]

Damien Mu
CEO and Managing Director
AIA Australia

Appendix

#	Proposal	AIA response
B4	We propose to: a) in our relief, retain a requirement that superannuation calculators must not be used to advertise or promote a specific financial product, and introduce a requirement that retirement estimates must not advertise or promote a specific product; and b) provide guidance on how assumptions relating to a specific financial product can be used without breaching the requirement not to advertise or promote a specific financial product: see draft RG 000.93–RG 000.96.	We do not agree with the requirement that superannuation calculators and retirement estimates must not be used to advertise or promote a specific financial product. Specific financial product assumptions need to be incorporated into these tools. Guaranteed income stream products are highly customised and specific to the product issuer and to the member's characteristics (age, gender, reversionary status and level of death benefit/withdrawal benefits guarantees offered). The alternative is to use reasonable investment and mortality assumptions for pricing lifetime income streams (e.g., assumptions we use in the actual pricing of our products) but that would differ from others in the market (e.g., we would not know specifically know what a competitor uses) and we would require clarity that it would not be deemed to promote a particular product. For a retirement estimate for a guaranteed income product to be relevant when comparing other income stream constructs, it needs to provide assumptions that are reasonable or closely aligned to the construction of the income stream product the member may elect to invest in.
B5	We propose to retain the requirement that retirement estimates may only be given to members aged under 67 who have been a member of the fund for the year ending on the date of the estimate. We propose to additionally require in the relief instrument that a retirement estimate must not be given to a member who: a) is in the retirement phase at the date of the estimate; b) has not made or received a contribution to their account during the year ending on the date of the estimate; c) has an account balance of less than $6,000 at the date of the estimate; or d) has a defined benefit interest in the fund.	We do not agree with the use of a default age of 67, as this should instead be aligned with the member cohorts developed by a trustee as part of their RIC strategy. Only if cohort-specific information is not known should a default age of 67 be utilised. The guidance should make it clear that trustees can promote the use of forecasts for those in the retirement phase – as recognition that members circumstances change over time and/or decisions made when first retired may not have been optimal This process should not be "set and forget".
C1	We propose to adopt a single framework for how economic and financial assumptions should be made for superannuation calculators and retirement estimates when relying on our proposed relief.	We support the proposal to adopt a single framework for how economic and financial assumptions should be made for superannuation calculators and retirement estimates and the flexibility proposed for providers to set their own reasonable assumptions.

#	Proposal	AIA response
C2	Under this framework, we propose to give trustees and other providers flexibility to set their own reasonable assumptions relating to investment earnings, fees and costs for superannuation products. These assumptions must be reasonable and certain disclosure requirements must be met: see draft RG 000.116–RG 000.128.	The flexibility to set different assumptions between forecasts is needed, particularly where the forecast may be comparing options where the member is invested in underlying products that provide a guarantee for some or part of their retirement income.
C4	We propose to update our guidance to explain how trustees and other providers can set reasonable assumptions.	
C5	We propose to update our guidance to state that we expect trustees who provide both superannuation calculators and retirement estimates will set assumptions consistently across these forecasts. There should be reasonable grounds for using different assumptions (e.g. tailoring assumptions for a retirement estimate based on an individual member's investment strategy): see draft RG 000.182–RG 000.183.	
C8	We propose to prescribe default assumptions for the retirement age (age 67) and drawdown period (25 years) that must be applied to superannuation calculators and retirement estimates: see draft RG 000.129–RG 000.132.	We support prescribing default assumptions relating to inflation. However, mandating a retirement age of 67 and a drawdown period of 25 years is likely to be inconsistent with trustee obligations to develop cohort-specific strategies. Funds can have very different demographics and there will be very different cohorts within the same fund. It also fails to account for females, who retire slightly earlier but have a materially longer life expectancy. Providers should have flexibility to set these factors based on the intended audience or member cohort. As noted earlier, modelling based on average life expectancy underestimates retirement outcomes at least 50% of the time and therefore is not credible for a significant portion of the intended audience.
C10	For retirement estimates, we propose requiring trustees to work out the annual income stream on the basis that the member would have a constant income from year to year, after inflation, for 25 years. This includes drawing down their lump sum on retirement to zero and taking into account the minimum drawdown rules: see draft RG 000.133–RG 000.140.	As noted, there are many factors that mean this is unlikely to materialise in the way it has been modelled. Providers should be required to provide appropriate disclaimers that note the limitations and encourage the member to access interactive retirement estimates or superannuation calculators to better understand their own circumstances. The risk of presenting an estimate that may appear sufficient on first perusal, but carries significant underlying risk of not materialising, is unlikely to lead to optimal decisions.