



COMMONWEALTH OF AUSTRALIA

# Official Committee Hansard

## SENATE

SELECT COMMITTEE ON SUPERANNUATION

**Reference: Portability of superannuation**

THURSDAY, 31 JULY 2003

SYDNEY

BY AUTHORITY OF THE SENATE

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**SENATE**  
**SELECT COMMITTEE ON SUPERANNUATION**

**Thursday, 31 July 2003**

**Members:** Senator Watson (*Chair*), Senator Sherry (*Deputy Chair*), Senators Buckland, Chapman, Cherry, Lightfoot and Wong

**Senators in attendance:** Senators Buckland, Cherry, Lightfoot and Watson

**Terms of reference for the inquiry:**

To inquire into and report on:

- (a) the extent to which portability of superannuation benefits already exists;
- (b) the role of current, and likely future, barriers to portability, including exit fees;
- (c) the desirability and practicality of the portability regime contained in the draft regulations, particularly in the context of the existing structures of the superannuation and financial planning industries; and
- (d) additional consumer protection measures.

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**Committee met at 9.06 a.m.**

**CHAIR**—I declare open this first public hearing of the inquiry by the Senate Select Committee on Superannuation into the portability of superannuation. Under its terms of reference, the committee's inquiry will focus on, firstly, the extent to which portability of superannuation benefits already exists; secondly, the role of current, and likely future, barriers to portability, including exit fees; and, thirdly, the desirability and practicality of the portability regime contained in the draft regulations, particularly in the context of the existing structures of the superannuation and financial planning industries.

Today, the committee will hear evidence from a range of individuals representing the following parties: the MTAA Super Fund, ASFA, AIST, IFSA, Watson Wyatt, the Queensland Local Government Superannuation Board, Australian Administrative Services, the FPA, and the Society of Superannuants.

All of the witnesses who appear before the committee are protected by parliamentary privilege with respect to the evidence they give. This means that witnesses are given broad protection from action arising from what they say, and that the Senate has the power to protect them from any action which disadvantages them on account of the evidence given before the committee. The committee prefers to conduct its hearings in public. However, if there are any matters which witnesses wish to discuss with the committee in private, we will consider their request.

[9.07 a.m.]

**WATSON, Mr Paul, General Manager, Superannuation, Motor Trades Association of Australia Superannuation Fund**

**CHAIR**—I welcome our first witness, Mr Paul Watson. Thank you for your submission. I invite you to make a short opening statement.

**Mr Watson**—I thank the committee for giving us the opportunity to provide a submission on the Superannuation Industry (Supervision) Amendment Regulations 2003, which I will refer to from here on as the draft portability regulations. I would like to pick up on some points covered in our written submission and make a short opening statement thereto.

**CHAIR**—It might be useful to highlight matters for the *Hansard* record so that the written record truly reflects your submission.

**Mr Watson**—Certainly. The Motor Trades Association of Australia Superannuation Fund is the national industry superannuation fund for the retail motor trades in Australia and as such is the predominant industry fund for motor vehicle repairers, dealers, petrol outlets, and the tyre, brake and kindred motor vehicle industry throughout Australia. The fund is supported by its principal employer sponsor, the Motor Trades Association of Australia, which is the national peak representative body for the retail motor trades and automotive industry. The MTAA superannuation fund have approximately 210,000 members, 32,000 employer sponsors and about \$1.6 billion in assets under management. We strive to maximise our members' ultimate retirement income benefits as well as provide them and their families with competitive death and disability benefits and other value added services throughout their working lives.

MTAA super have previously stated, in evidence to earlier choice of fund and related Senate inquiries and in other public forums, that we support the objective that all Australians should be members of efficient, well-managed and prudentially run superannuation funds which are appropriate to their needs for retirement. That said, MTAA super also believe that the earlier rejections of the various iterations of the choice of fund bill since 1997 have so far been done for good public policy reasons, and our reasons for saying that are on the record. We continue to maintain that a number of the disconcerting elements of the previous bills relating to choice remain to be adequately addressed. We are also of the view, as I will expand on this morning, that the draft portability regulations do not in isolation address these concerns, which we also argue are largely common to both the portability regulations and the choice of fund mechanism. MTAA super argue in our submission that the draft portability regulations have a real potential to be detrimental and counterproductive to the outcomes actually sought by the government in bringing the regulations forward.

If the draft regulations solely dealt with the ability to transfer existing inactive account balances to a person's current superannuation fund—that is the fund to which mandated superannuation contributions or other contributions are currently being paid by a current employer—then this would be a very positive and cost-saving initiative and one that we would thoroughly support. But, at the same time, one would question the need for such regulation

where the existing law allows for such rollovers to occur now such as when a person leaves one employer to join another. That is a trigger event under the current legislation and allows a person to roll over an old employment linked super account balance to their current superannuation account.

In our experience, some of the existing barriers which prevent people from availing themselves of the current ability to do that are a result of a number of factors. One is, in the vernacular, good old Aussie apathy, of which we have all heard evidence before. Also, there is certainly evidence that some funds will deliberately frustrate a member's attempt to roll over or transfer a benefit from one fund to another. There is also the cost of doing so and I particularly refer to exit fees, which are a real issue to be dealt with. As an aside, recently I have come across transfer values where people have sought to move money from an existing superannuation account where they were counselled not to effect that rollover simply because to do so would trigger exit fees. In one case, a \$6,000 balance required a \$5,600 exit fee, so that is the equivalent of 93 per cent. There was another case where a person's balance was \$1,300 and the exit fee was \$1,200, so that is also a 93 per cent exit fee. At the other end of the scale, a \$217,000 account balance required a \$41,000 exit fee, which is equivalent to approximately 20 per cent of that balance. These are very contemporary examples of exit fees in the marketplace, so there is still quite an issue that needs to be dealt with there.

If the draft portability regulations were more particularly to address these issues in relation to the transfer of moneys under the existing trigger events, we believe that this would be most welcome and we would support such initiatives. However, the reality of what is before the committee today is quite different. In our view, and I believe the view of a number of witnesses you are yet to hear from, portability without the complementary choice of fund arrangements—suitably amended in our view to more particularly consider consumer protection and other safeguards as we have previously well documented—has a real potential to lead to a proliferation of inactive accounts, which is quite the opposite to the intention of the regulations. Also, we fear that a siphon effect could readily develop where fund members are encouraged by third parties to regularly transfer money from their employment related superannuation fund to another such as a retail public offer fund on the strength of a third party's advice, which could well lead to an increase in the number of lost and inactive accounts over time. Also, increased difficulty for trustees would develop in determining long-term investment strategy and business planning on the strength of their membership base and the scale of funds under management, which currently deliver the ability for funds such as ours to negotiate and secure deep wholesale supplier arrangements. In addition, the payment by members of overly high fees in total may occur as a result of simultaneously operating two or more superannuation accounts.

MTAA Superannuation also holds the view that, without the previously highlighted, well-documented and discussed inadequacies of the choice of fund proposal as presently structured being substantively addressed, portability effectively represents an opportunity to introduce choice of fund by stealth. If the portability regulations were enacted as they presently are, we believe that this would create an unacceptable situation whereby an employee could direct their super fund to transfer their account, or part of their account, to another fund largely at will but where the person's employer could still determine where the next superannuation instalment is to be paid, which may be to a different account. It would be hard to argue though, politically and practically, in such a fractured environment, that choice of fund would almost certainly need to be enacted without delay in order that the ghosts of contributions past, being portability and, in

the future, being choice of fund, do not cause the member, their fund or their employer untold administrative angst or cost.

Put more simply, an argument can be made that portability is a Trojan Horse through which it is possible that the choice of fund bill, as it is, can be fast tracked and passed so that the two complementary parts—portability and choice of fund—are brought forward together and simultaneously, but without portability having the protection rights and mechanisms that we have sought in choice. As such, MTAA Super strongly supports the portability of superannuation benefits and the choice of fund provisions being amalgamated and dealt with as a stapled package of legislation. That is, one fundamental element of the overall proposal cannot be introduced without the other complementary proposal.

Turning now to the draft regulations, we have outlined in our written submission to the Treasury and to the committee that if introduced in isolation to choice of fund proposals, suitably improved, portability would effectively create a disconnect between the fund to which an employer contributes mandated superannuation on behalf of an employee and the fund to which that employee considers to be their active or primary fund which could be two different funds, or more, altogether.

MTAA Super, in its experience, believes that such a situation would simply lead to a proliferation of small, inactive accounts; a higher churn rate between funds resulting in higher costs for members and funds; and a potential reduction in the ability of funds to provide highly competitive and advantageous group life insurance benefits and arrangements. An analogy that helps to underline this outcome is the situation where legislation is passed allowing people to move—as they can—their bank account balance between banks at will, but where the decision as to where the person's next pay packet is to be paid is left solely and utterly to the employer. That would be unworkable and we would argue that a similar situation would be created if the portability regulations were enacted as they presently are without the choice of fund legislation being appropriately improved and brought forward as well. Nobody would sensibly advocate that situation but that is effectively what the Senate is being asked to look at and to do in respect of the existing superannuation account balances and future contribution payments that these two instruments allow or propose to allow.

The government also argues that the introduction of the portability arrangements will allow people to extricate themselves from poorly performing funds. In our experience, very few fund members are effectively disenfranchised or economic conscripts to poorly performing funds, mainly because, if their fund is performing so badly, their employers will almost always take steps to roll those members out of such inadequate arrangements notwithstanding any industrial relations awards or other hurdles that may prevent them from so acting. As such, MTAA Super does not believe that the portability provisions on balance represent a net improvement in people's overall circumstances in respect of such situations.

In our written submission, MTAA Super describes other issues which we argue also require further consideration by government in respect of its portability regulations. These relate to member protection; the frequency of rollovers; the possibility of arbitrage between rolling over between funds; liquidity of investments and long-term nation building investment strategies by super funds being affected; and the issue of education, consumer protection and disclosure. Those are the key issues. Curiously, it has been speculated on and reported that the

superannuation industry is far less concerned about the introduction of portability than about the choice of fund. MTAA Super believes that this is a falsely drawn conclusion based primarily on the lesser level of disquiet exhibited by the many stakeholders who have participated in consultations and roundtables, and presented evidence to this committee, on choice of fund issues rather than on portability.

The key reason portability has not been as keenly scrutinised and debated to date is because we believe the majority of the industry stakeholders have always believed, logically, that the related issues of choice and portability would be brought forward together and conjoined so that the issues of selecting and moving between super funds could be further considered concurrently given the utter commonality of the issues surrounding both portability and choice of fund issues.

Again, this only serves to underpin the MTAA Super recommendation that the issues of portability and choice of fund be formally conjoined for the purposes of further and, hopefully, final consideration by the parliament, the industry and ultimately the members of super funds so that these highly correlated issues can be properly examined, debated and considered. This would allow the parliament to better understand and judge the effectiveness of the existing options and mechanisms available to fund members and their employer sponsors in respect of the transfer of superannuation between funds rather than having the current proposed choice of fund and portability prescriptions imposed which may overly and unnecessarily add to an already complex web of superannuation regulation in Australia.

In the interests of time and the committee's busy schedule, I will conclude my oral remarks at that point, but I would be pleased to expand on anything I have said here this morning or in our written submission. On behalf of the trustees and the members of MTAA Super, I thank you for this opportunity to again address you.

**CHAIR**—Thank you, Paul. What was the reaction of Treasury to your concerns? Have you had a written response in relation to the sorts of issues that you have raised with us if you raised those same issues with Treasury?

**Mr Watson**—No, we have not had a response from Treasury.

**CHAIR**—Did you have a face-to-face discussion with them?

**Mr Watson**—No, surprisingly.

**CHAIR**—You just sent them a letter?

**Mr Watson**—We provided the submission and offered to expand on or to discuss the issues raised in our submission with Treasury. Given that we are physically less than half a kilometre from Treasury, it would have been fairly easy for us to have responded to any invitation to further expand on our written submission.

**CHAIR**—Did you seek an opportunity to discuss it with them face to face?

**Mr Watson**—No, on this occasion we did not. I think that may have had something to do with the time between when the submission went to Treasury and the decision for a very short and sharp inquiry by the Senate into the same issue.

**CHAIR**—Okay. I refer to those funds with a 93 per cent or 41 per cent exit fee. I could stand corrected on those figures. Are those funds very old funds or are they more recently established funds?

**Mr Watson**—My understanding is that the funds that I gave evidence about with a 93 per cent exit fee were funds that I suppose we could now call somewhat old-fashioned in terms of being linked to life insurance policy as well. But some that I am aware of are what we would probably call, certainly since 1992, straight accumulation type arrangement funds but where the exit fee is quite heavily skewed to the back end of any transfer. I gave evidence about a balance of about \$1,300 where there was a \$1,200 exit fee. In that particular case, my understanding is that the size of that exit fee pretty well related to the trail commission to be paid to a third party in the first 12 months of that policy's existence.

**CHAIR**—That trail commission would have well and truly been honoured at this stage, wouldn't it, if it was an old fund going back to 1992?

**Mr Watson**—In that particular case, I think that was a fairly new policy and that the high exit fee represented, in effect, an early transfer penalty because of the need for the product manufacturer to honour the initial 12-month fee to the intermediary.

**CHAIR**—Obviously, this is a problem. How can government overcome a contractual arrangement between the person who takes out the policy and the company? Surely we just cannot pass a law banning—

**Mr Watson**—Protecting people from commercial—

**CHAIR**—Yes.

**Mr Watson**—Absolutely. But, as we have been on record as saying in terms of choice—

**CHAIR**—What is the way around it?

**Mr Watson**—Certainly we cannot do anything retrospectively but, in moving forward, we and certain others have proposed that one protection mechanism would be that, if there were a cap or a legislated ban on commissions or trails being paid against mandated superannuation contribution payments—and now I am talking about superannuation guarantee and/or award payments—then I think we would certainly see those high back-end loaded exit fees drop away simply because if there is no trail or commission payable against those sorts of contributions—

**CHAIR**—There would be no justification?

**Mr Watson**—Exactly: there would be no justification for the exit fee. You raise a very pertinent point. If, for example, a person consulted a planner and wished to put away some discretionary superannuation savings outside or over and above any employment related

superannuation—I agree with you completely—in a sense caveat emptor would apply. That is where another arm of the argument comes in: what is needed is a generational education and awareness campaign on superannuation and retirement incomes, with FSR and other initiatives coming on stream, to better arm people to understand and ask up-front what these costs may involve.

As for people seeking to make voluntary contributions to superannuation and to choose a product that best suits them, I agree with you: there is probably not much that we could or should do to interfere with commercial arrangements between a person and the counterparty. But we do take a rather paternal view, in a sense, with mandated superannuation because we know from vast experience with our membership, many of whom are on AWOTE or less in terms of income, that the superannuation they receive from their employer is their one shot at some semblance of a retirement income outside the age pension. We feel rather protective towards making sure that that is not whittled away or in any other way diminished through excessive fees.

**Senator BUCKLAND**—In the overall picture isn't it better that funds all stay in the one pool?

**Mr Watson**—Absolutely. When you say 'funds all stay in the one pool', we are certainly concerned at the potential churn rate between superannuation funds that the current portability regulations, we believe, would certainly see occur. The issues with the current choice of fund bill require addressing to try to counter that, in the sense that we are fearful that, human nature being as it is, we will have a number of members in superannuation funds in Australia chasing last week's, last month's or last year's top return. As we all know, in a survivor bias in the tables, very few of those who were at the top of the pile a year or three years ago are there now, simply because of style bias and the oscillation of markets. Very few funds will be consistently top-performing funds. If people are constantly fund hopping to chase return, it can be quite detrimental if, on the way through, a little piece is taken each time, or in some cases quite a large piece, in fees and charges. That leads to another issue about the life insurance issues that that also impacts on.

I will give you a quick example. We have, by independent analysis, one of the most cost-effective group life insurance policies being offered by super funds. Our insurer would insist on a complete re-rating of the costs if we had a churn of membership of about 25 per cent of membership in any given contract period. Whilst that churn of membership would be very remote in the current market, if people were basically allowed a mechanism that allowed them to siphon off and to move superannuation at will, for no other reason than selecting funds for certain benefits—maybe a bit in this fund for its insurance arrangements, and a bit in this fund because it might offer a particular investment choice they are keen on—those churn rates could easily be achieved and there would be a distortion and a change in the group insurance market. It would effectively mean individuals being underwritten in a retail sense again, and the costs would be larger for a fund member such as ours.

**Senator BUCKLAND**—You mentioned in your submission that there should be a 12-month period before you could make a second change. I think that is what you basically said.

**Mr Watson**—That is right.

**Senator BUCKLAND**—Have you any statistics from your fund to indicate what the likelihood of fund change would be? Is there any evidence to suggest that it would happen?

**Mr Watson**—Not from practical experience. We would draw on the experiences that we have probably all witnessed in the UK and Chile and in other markets where effective deregulation of a sense occurred and where third parties became very active in encouraging people to change funds—some for good reason if the fund was a poor performer in a number of fields, but quite often for motives other than purely what was in the best interests of the member. From our experience and research, churn rates of 20 or 25 per cent are not uncommon where those occurred. In terms of our own fund, no, we do not have exit rates of anything of that nature at the moment, hopefully, because we would like to think we are a fairly well-performed and well-managed fund. But you cannot guard against what people may be advised to do for other reasons should the opportunity, in terms of a change in legislation, allow it.

**CHAIR**—Have any of the employer members of the organisation raised this question with you—that they have had inquiries from members?

**Mr Watson**—The employer sponsors who have approached me, either directly or through associations such as the Motor Trades Association, the Small Business Coalition and the like, have certainly been very fearful of what I would loosely call the carpetbaggers. I will give you an example regarding choice of funds in 1997-98. The market saw that it was quite likely that the legislation could have been passed at that point. We saw quite a fever of activity in the marketplace, particularly from the bigger end of town in terms of the larger retail funds. With marketing, advertising and the dealer network activity that occurred in the ramp-up to what was considered to be the most likely point at which the legislation may have been passed, I can readily recall that at the time several banks with household names had saturation-type coverage with the advertising of products they were bringing to the market because of what looked to be the deregulation of superannuation.

That caused great consternation amongst our employer sponsors, mainly because they saw the current mechanisms as working quite well. Particularly with the Motor Trades Association superannuation fund, even though we are named in several federal awards relating to the retail motor trades in Australia, I have met plenty of employers who, if they did not think we were doing a good job, would not hesitate to step outside the award and contribute to another fund if they thought that fund was superior and more in the best interests of their employees than our fund.

**CHAIR**—How do they stand in that situation? Would they be in breach of the award?

**Mr Watson**—As the fund is not technically a party to the award—we are named in it—there is a question mark over enforceability of the fund in terms of an employer contributing to the award. But that is certainly something that the parties to the award, being the employer associations and the member representative bodies—the ACTU or, in this case, the AMWU—will from time to time talk about, negotiate and enforce. I will relate another story from that time. As an association—and through it the MTAA superannuation fund—we were asked by employers to advise on and consider preparing simplified one-issue workplace agreements relating to superannuation should that bill have become law at the time, simply because they wished to negotiate and agree with the employees that the status quo applied. Everyone was

happy with that arrangement and they did not want employees or the employer to be constantly answering the door to sales forces seeking to sell their products and their superannuation arrangements as opposed to the one that they were currently in. They were quite fearful of the activity that they were to be subjected to.

In fact, being a nationally based industry superannuation fund, we did see some evidence of that in jurisdictions where choice of fund does effectively apply, which is predominantly in Western Australia but we have also seen instances of it in Queensland and South Australia. In fact, we have had reports from South Australia of the sales representative of one particular company visiting employees with the company solicitor in tow so that they could write there and then an agreement that could circumvent all the things being proposed in the choice and portability rules. That is the marketplace.

**CHAIR**—Coming back to your submission, you indicate that you would be happy with portability, in bringing all those funds together into the main employment fund at the moment. What about if I have a choice of six funds and I nominate one fund from within the six for the purpose of consolidation? Would you have any worry with that?

**Mr Watson**—We would.

**CHAIR**—It would be reducing the cost.

**Mr Watson**—Agreed but, in part, the answer to this is that we would also have to go back and talk about default funds and the arrangement that applies to them.

**CHAIR**—No. The employer continues to provide money into the main fund, which is the default fund for the purposes of a company. What would be wrong with regulations that allow a person to consolidate into one of his existing funds? It may be the employer fund or it may not be. I am asking what is wrong with it not being the employer fund?

**Mr Watson**—I will give an example of where we see difficulties in that scenario. Let us say that you did have six funds and let us call fund No. 1 your current fund, to which your employer is contributing. But fund No. 3 is the one in which you would prefer your contributions to accumulate—one of the other six funds as you were describing.

**CHAIR**—Yes.

**Mr Watson**—In that situation, our concern would be that siphoning effect that I described a little earlier. As the regulations are currently written there is little, if anything, that I can see that would prevent the employee from having a standing instruction with us—let us say that the MTAA fund is the current employer contribution fund—that on the last day of every month they submit a form to instruct us to move the contribution made that month from our fund to their preferred fund. In other words, a person could be operating a sink fund, very much like a transaction at-call bank account.

**CHAIR**—There would have to be that protection built in. Provided the protection was there that did not allow a siphoning off from your existing employer contribution fund, what objection would you have?

**Mr Watson**—The only objection I would have is that there would need to be a mechanism that would, in effect, prevent a superannuation fund being used as an at-call bank account; it is an entirely different account. I know that in some of the submissions provided to the committee there has been some suggestion of an annual cap being placed on how often a person might effect a partial transfer between accounts.

**CHAIR**—That could be sensible.

**Mr Watson**—That certainly has some merit and would go some way towards addressing that siphoning off effect. Again using our own fund as an example that I can speak to, we did away with any form of exit fee quite some time ago. To address the equity between members we would have to seriously look at re-introducing a processing fee for such a transfer so that equity between members was maintained.

**CHAIR**—If you allow complete portability, I can understand that.

**Mr Watson**—I made the point in our submission that, if the portability regulation primarily dealt with the ability for people to move inactive accounts to their primary active account, that would be very positive. I do not think you would have a word spoken against that. But I also point out that I am not sure why—and nobody has been able to point me to it anywhere in the SIS legislation—that cannot occur at the moment. For instance, leaving one employer to join another is a SIS trigger event which would allow the previous account balance, unless it was a certain defined benefit or maybe a public offer exempt fund, to be transferred and amalgamated, in a sense following the employee to the new employer.

So I question whether these regulations actually improve on that situation. Again, it probably comes back to the education issue. I am fearful that in the current format before you today there would be an open slather ability for people to literally move a contribution from one account to another almost as it is being made. As I said, that will affect a whole range of things that that fund, to this point, has assumed in terms of its calculations for its long-term investment strategy. We have not yet spoken today about the affect that that would have on the liquidity of funds. I think some witnesses to come after me today will talk in more detail about that. Certainly I can say from experience that we are one particular fund that has very long-term, patient capital investments, particularly in nation-building type assets and infrastructure—that being hospitals, power generation, roads, transport and the like. We have a prudential obligation to look very seriously at our liquidity and investment levels if we were not sure about the churn rates and membership balances within the fund.

**Senator BUCKLAND**—At the inquiries we always have a bit of a run on the issue of education of members, and I think you have mentioned that issue in the past.

**Mr Watson**—I have indeed.

**Senator BUCKLAND**—I suppose we ask this question all the time, but it has to be asked: do you think there is sufficient knowledge among employee members of funds of the exit, entry and other fees associated with the transfer of partial funds or whole funds? Do you think that the education as it is now sufficiently addresses the matter of the members' understanding of the liquidity of the fund?

**Mr Watson**—Unfortunately, the answer to that is no: I do not think the levels of education of the typical member are such that an informed decision can be made or that they are making those sorts of informed decisions. I base that on a couple of things. One is pure and utter experience with our fund. I gave some examples of transfer values which were unbeknown to the person seeking to roll funds into our fund, and I know this happens with other funds as well. We, along with a number of funds, run an advice service where we provide people considering transferring an account balance from another fund to our fund where we look at the detail of the other fund, its fees and exit fees, and present them with a cost benefit analysis. I have given you some examples where we clearly provided advice to a member not to transfer to the fund because the cost of doing so, in our belief, was exorbitant and prohibitive.

Members are disappointed when they cannot amalgamate the balance because of such an impediment, and you can imagine what their view of superannuation is when they go back to the workplace. Their negative view is like a virus and it permeates that workplace to the point where there is a negative view of superannuation as a retirement savings product. I think you only have to look at the most recent APRA statistics to see that the discretionary savings in superannuation have dropped. That is partly due to the markets and the returns we have seen in recent years but, from first-hand experience, I can also say that it is because Joe Public has a very dim view of superannuation at present as a retirement savings product—and that is because of this and a number of other reasons. The education factor is such an important one. As in any situation, an informed person is going to make informed decisions. However I do not subscribe to the view that we can throw a lot of money at the tax office and have an information campaign which in six or 12 months will improve that. The education campaign that has to occur in terms of superannuation and retirement savings is generational—it is going to take that long—but we have to start somewhere.

**CHAIR**—We have to start educating young kids.

**Mr Watson**—Exactly. I could go on all day about this. I think it needs to be in the curriculum in schools, it needs to be taught in universities, it needs to be taught in the workplace, it needs to be done by funds and it needs to be done by government. No one entity is responsible for carrying that education campaign. It has been very interesting reading this committee's report on retirement savings, which was released this week. There are issues in there which are very similar, in terms of people understanding and knowing what retirement incomes, pensions and the like are going to be like. At the moment, they are very reliant on third parties to provide that advice. It comes around to how we can best protect people and make sure that the advice that they do get—because, let us face it, until that educational bar is lifted, there is going to be quite a need for external third party advice—is as untainted and as utterly in the interest of the advice seeker as we can make it.

That brings me to one more point: what can we do now to assist the situation? I believe—in a sense, what I described our fund as doing—that the portability regulations could be improved by also insisting that, if there is a transfer to be made of a partial account balance, the fund provide a cost impact statement to the person. So if a person makes an inquiry of their superannuation fund and says, 'I wish to transfer my balance to another fund,' I think that person should be provided with a cost impact statement as to what that transfer would cost them, so that all fees, exit charges and the like are provided with the benefit quote. I think that will assist people. If they see the figures that I have described earlier, that might sooner help the educational situation.

**Senator CHERRY**—What are the current rules for portability out of your fund?

**Mr Watson**—As long as a person has satisfied a trigger event per SIS, so it meets the legislation, and there is not an active employer contribution being made to that account, a person could exercise a choice to transfer their balance to another fund. The key there is the employer contribution. If a person says to us, ‘I wish to transfer my balance to another fund,’ our first question to them is, ‘Have you ceased employment with your current employer, who is making contributions to the fund?’ If the answer is no then we cannot transfer that balance as it presently stands without the employer turning off the tap. Otherwise, if an account is transferred and the employer is still paying, that raises a whole heap of implications for both the fund, the employer and the member.

**Senator CHERRY**—And that is your principle trigger—you do not have an industry trigger as well?

**Mr Watson**—If they are moving outside the industry?

**Senator CHERRY**—Yes. If they are likely to be re-employed in your industry, do you require them to stay in your fund?

**Mr Watson**—No, not strictly. As I mentioned, if we have an employer contributing pursuant to a federal award then we are one of four or five funds named in the award. So the person could quite readily be transferring their account, say, from the MTAA Superannuation Fund to, say, the Australian Retirement Fund, another award named fund. That completely and utterly continues to meet the award obligations of the employer, and that would be quite within their gift to do.

**Senator CHERRY**—Even if we do proceed with a regulation, do you think it should allow for partial rollovers at all? That is one of the most surprising things I saw in any regulation.

**Mr Watson**—Our view is that partial rollovers will actually create the opposite effect to what the regulations are seeking to do in terms of reducing the cost, increasing competition and improving the lot of members. For the reasons that I have given earlier, we think that partial account transfers will actually increase costs, because funds will have to recover the actual cost of processing the transfer, and I think that any cost should be absolutely limited to that direct recovery and nothing more. Again, it is that churn factor. We believe that it would lead, over time, to a proliferation in account numbers. If people are moving around, it might be on the advice of a third party. They might get further advice from someone else, and that advice might be to transfer to another fund. As we have seen in the past, and the reason we have mechanisms like the lost members register and the SHAR, it comes back to that issue of Aussie apathy. People just either forget, or are not that interested at that stage of their life in, where they have put pockets of super.

**Senator CHERRY**—How long would it take your fund to process a request to shift their account balance across somewhere?

**Mr Watson**—If it were what I would call a cleanskin account—there were no residual issues with insurance premium payments and it was a clean transfer—I suspect that well within 30 days would probably be an achievable transfer period. If there were any issues with the account in

terms of chasing up arrears of contributions owed to that account or any issues to do with premiums on insurance payments, 60 days would cover 95 per cent of cases.

**Senator CHERRY**—What sorts of cases would push out beyond that and take longer?

**Mr Watson**—Quite certainly cases where we might be in arrears recovery action with an employer, so there are still residual monies to be paid into that account, or SG money where there is an arrears to the account that we are pursuing on behalf of the member. That would probably be the primary one. The key delay is where there are still outstanding contributions to be receipted to the accounts. In terms of the paperwork, the other primary reason that delays occur is where members have not provided all the necessary information about the receipting fund. By law we must make ourselves comfortable with the fact that the receiving fund is a regulated fund under SIS and the like, so sometimes there is a need to chase up small details that the member has not made.

**Senator CHERRY**—How would you define an active fund for the purposes of a regulation?

**Mr Watson**—I define an active fund as a fund into which the person's current employer is contributing superannuation on a regular basis pursuant to an award, the superannuation guarantee regulation, an Australian Workplace Agreement or a Certified Workplace Agreement. It is a fund into which mandated superannuation of one form or another is being contributed. I draw that distinction about a superannuation account that a person may open into which they want to put discretionary separate savings. The active account could also be one into which salary sacrifice contributions are made, because under the current law they are, for all intents and purposes, made as an employer contribution as well. That would be my off-the-top-of-my-head definition.

**CHAIR**—An industry like yours employs a fair few casuals. Does that change the notion of an active versus an inactive account?

**Mr Watson**—Again, even for the casual employee, it would be the account to which an employer or several employers are contributing at the time they are drawing income from that source. You could well find a situation in a casual sense where they may choose quite deliberately to maintain two or three funds across two or three jobs. As Senator Watson said earlier, they may wish to use one of those as a primary account to accumulate those balances in the long term. There may be reasons, of an award or other nature, that at that present point in time they cannot have the other two employers contributing to that one account. That comes back to why I say that portability is the left hand; choice is the right hand. Having the two disconnected is going to create quite some trouble between where employees wish their money to be and where employers wish to pay it. That comes round to the situation where, if you allowed, say, an annual account transfer, a casual may wish to move small balances from two other accounts to a primary account.

**CHAIR**—Thank you very much, Paul.

[9.54 a.m.]

**ANDERSON, Dr Michaela, Director, Policy and Research, Association of Superannuation Funds of Australia**

**HODGE, Mr Robert, Senior Policy Adviser, Association of Superannuation Funds of Australia**

**CHAIR**—Welcome. Thank you very much for your submission. We ask you to speak briefly to it.

**Dr Anderson**—Thank you for the opportunity to be heard on this important matter. ASFA's submission outlines our views. I will very briefly summarise them because you have heard already this morning much of what we would say. It is ASFA's view that portability provisions are essential to complement any choice of fund provisions. Choice of fund would provide the opportunity for employees to choose the fund into which mandated employer contributions are paid. Portability provisions would allow them to move existing benefits into a fund of their choice. To implement either of these provisions without the other presents some problems, not least of which is the potential to increase the number of accounts held by each member, not reduce them. If only choice of fund legislation is introduced, employees who choose a different fund for future contributions may be unable to move existing account balances—that is, they will have two funds if there is no portability mechanism. If only portability is introduced, employees could move their existing account balances to a new fund but the employer may continue to pay into another fund. Again, the employee has two funds at least. There is a suggestion that portability will assist in addressing the issue of multiple superannuation accounts. On its own without choice legislation there is no basis for that statement. If we think it will address the large number of inactive or lost accounts currently in the system, there is again no basis for this optimism. There are no legal impediments to the owners of this lost money sweeping it up into current accounts.

Failure to consolidate is a behavioural problem, not a legal problem. Portability without choice could become a backdoor version of choice: the employer pays contributions into a fund and the employee systematically channels them into a different fund. This is a model which could be adopted. However, if this model were adopted, if portability were introduced without choice of fund legislation, then consumers would still need an effective disclosure regime and adequate financial skills to choose another fund, issues which we are still looking for in choice of fund. In a portability regime, as in a choice regime, uninformed consumers would be vulnerable to unscrupulous people interested in their own wealth creation, not the client's. A backdoor choice model does not let us off the hook in consumer protection. While I was sitting listening to the first person presenting evidence today, I looked up at this window here. If you look really closely at it with new glasses, as I have, you will see that it says, 'Knowledge is the mother of wisdom and virtue'. I do not know about the virtue but I am quite certain that knowledge is the mother of wisdom. So knowledge is something that we really need to provide to those people who are going to choose another fund, either in a direct choice of fund regime or in this indirect backdoor version of choice portability.

I wish to correct an error in the ASFA submission. Gremlins inserted a very strange line in the text, and a corrected version has now been made available to you. Our submission made a number of observations about specific items in the draft legislation and we are happy to answer questions about these or any more general comments. Thank you.

**Senator BUCKLAND**—As we move towards retirement, do you see any real benefits to overall national society by introducing the portability of funds? Is this going to ease the burden on retiring people or is it going to increase the burden on them? If you introduce portability, what cost impact is it going to have on the overall finances of our nation?

**Dr Anderson**—If you introduce portability without choice?

**Senator BUCKLAND**—Yes.

**Dr Anderson**—We make some observations in our submission about some of the interesting fee implications for individual members. I think it was mentioned earlier this morning that when people are able to move out, other than when they leave employment, you may have to revisit some of the exit fees. In some funds those exit fees have been completely eliminated. I think you might have to look at that fairly closely.

**Senator BUCKLAND**—I will struggle a little further with this, if I may, Doctor.

**Dr Anderson**—Yes.

**Senator BUCKLAND**—If you had portability, would it affect the cost of retirement to the nation? At the moment we are trying to get people into superannuation to replace large parts of their draw-on pensions that are funded by the public purse. Eventually that is where we would all like to see it going. Will opening up portability contribute in any way to that?

**Dr Anderson**—I suppose you would have to argue that any increased administration costs were offset by greater or better selection by people of better funds. I am not quite sure that you can really say at this point that people are going to select better funds than those that they are currently in. There will be cases where, if they are selecting the flavour of the month, they may increase their earnings, but overall I am not sure you could say that the administration costs are going to be outweighed by people putting themselves in better earning funds.

**Senator BUCKLAND**—Do you have any evidence at all to suggest that there would be fund-hopping to any large extent if portability came in?

**Dr Anderson**—I have no direct Australian experience.

**Senator BUCKLAND**—What experience do you have?

**Dr Anderson**—I think you would have to look at not so much portability but choice in other jurisdictions, such as the UK and especially Chile, where there was a lot of churning. I find it fairly difficult to talk about portability without choice. Part of the problem that I have in answering your questions is that the two are so intrinsically linked. If you have portability and you do not have choice, there are problems. The same applies the other way around: if you have

choice without portability it does not make sense. Really, logic says that we should be talking about both of them together.

**Senator BUCKLAND**—Overall, do you think that having portability without choice would put members of funds at risk in that they would not be making informed and careful decisions?

**Dr Anderson**—That was the point that I was trying to make originally. If we are going to just introduce portability and not choice then we really need to put in the same protections that we would put in if we were going to introduce choice. It is choice; it is just different and it has the potential to be thought of as more benign.

The feeling I get is that government seems less worried about this part in terms of consumer protection, but I cannot see the distinction made between consumer protection needed for portability and consumer protection needed for choice. In both instances, people are going to be choosing a fund somewhere. It is at that point, I suppose, that we need to actually look at knowledge being the mother of wisdom.

**Senator BUCKLAND**—The final question I want to ask you—and I had not read that until you pointed it out to me—is: do you think that, if one was introduced without the other, it would open the doors for some operators that we might consider unscrupulous or those looking for a quick buck to come in and try to get people to hop around the different funds?

**Dr Anderson**—I think unscrupulous operators will be there, whether we introduce them together or separately. The issue is that we have to protect people and give them a defence against the dark arts.

**Senator BUCKLAND**—You heard Mr Watson's evidence earlier on. He made, in my view, a very valid point that the education in relation to superannuation should be part of the curriculum. Do you have a view on that? Do you support that view?

**Dr Anderson**—Yes, definitely. As a former teacher, I have a lot of sympathy for that and I am also aware that we have very crowded curricula. It seems to me that you have to fit it into things that are already there. Why it is not already in certain parts of our curriculum, I just do not know. I think we have probably a big education campaign with teachers to let them see where it fits into things they are already teaching.

**Senator BUCKLAND**—I think some of our teachers may well not have the ability themselves and that could be part of our problem.

**Dr Anderson**—I think so. I think that we need a 'train the trainer' sort of thing.

**Senator CHERRY**—I have just a couple of questions. The first is regarding exit fees. You indicate in your submission that 'ASFA supports the absence of a restriction on exit fees where these fees reflect the cost of processing'. What do you think is the cost of processing and what do you mean by processing?

**Dr Anderson**—I mean what it actually costs to have somebody go through the mechanics of the exit. It was interesting listening to the MTAA earlier talking about delays in transfer and

what that might be. You could see there that, in some cases, there is a lot of activity that has to go on. Generally speaking, they do not charge an exit fee, but you could make a case that there would be a small exit fee there. For some people, there would clearly be some subsidising where it really is a lot of work to get things in place to make a clean exit.

**Senator CHERRY**—You indicate that there are differing charges for active and inactive member accounts. Do you have any examples of those to hand?

**Mr Hodge**—Off the top of my head, for an inactive account, some industry funds would charge a weekly fee of, say, 60c for that account.

**Senator CHERRY**—In administration charges?

**Mr Hodge**—Yes, whereas for an active account it is typically \$1 or \$1.20 per week.

**Dr Anderson**—Our point, I think, in that part of our submission was looking at—

**Senator CHERRY**—Partial rollovers.

**Dr Anderson**—Yes, where someone is using the fund as a siphoning mechanism, they are not closing business with you and you were still having to maintain something. Funds would have to look very carefully at that, because there would be some inequities being developed.

**Senator CHERRY**—Do you support the notion of partial rollovers?

**Dr Anderson**—On the face of it, no.

**Senator CHERRY**—What is broken about portability at the moment, do you think? What are the current legislative restrictions to portability?

**Dr Anderson**—If you are in employment and contributions are still being made for you, then generally you cannot move that account. If you have left employment, then there is nothing except your own ability to get moving and make the decision. There are a couple of exceptions to that. I would think that we do not really want to go into the public sector ones where it is a defined benefit scheme and it is better for you to keep them there. Certainly in the New South Wales public sector if you take the withdrawal benefit, which you can at any time and you do not leave it there and get the full accrued benefit, you would have to have a very urgent need for that money because you are really doing yourself out of a lot of money. Exit fees, which are really not exit fees but penalties, might stop people. But these are not legal problems. Once someone has left employment and there are no longer contributions being made by the employer, then it is easy. In fact, funds are trying to make it easy for members to consolidate at that time when they arrive in a new job with a new fund.

**Senator CHERRY**—Have you received any complaints from members about the issue of delayed transfers and so forth or the cost of transfers?

**Mr Hodge**—I handle the general inquiries and very rarely do I get a complaint of that nature. When I do get a complaint usually there is some genuine reason, like lost paperwork or difficulty

in determining whether in fact it is an active account with employer contributions still coming in or not. Quite often where these have occurred, the delay has been the fact that the employer has not formally advised the fund that the member has ceased employment.

**Senator CHERRY**—Dr Anderson, I want to come back to your argument that consolidation is predominantly a cultural problem rather than a legal problem. I am an unreconstructed social engineer—always keen on trying to change culture by forcing people to change behaviour. What do you think we need to do from a policy point of view to get consolidation cracking, if this is not the way to do it?

**Dr Anderson**—There have been some suggestions floated around about automatic consolidation. Although, I am drawn to that in my unreconstructed social engineering phase as well—

**Senator CHERRY**—As a former teacher.

**Dr Anderson**—I do see that as having some problems which we would have to discuss very carefully before we move down that path. It does seem to assume that people are not capable of doing what they ought to do if we give them proper chances, and I do not think we have quite excluded that. The ATO has been going through some matching exercises with some of the funds. I probably feel more comfortable with that approach at this moment, rather than going with a compulsory consolidation.

**CHAIR**—Thank you, Dr Anderson. We have read your submission with interest. The committee will take a short break and we invite everyone to morning tea.

**Proceedings suspended from 10.14 a.m. to 10.39 a.m.**

**ROBERTSON, Mr Ian Alexander, Secretary, Australian Institute of Superannuation Trustees**

**RYAN, The Hon. Susan, President, Australian Institute of Superannuation Trustees**

**CHAIR**—I call our next witnesses, from AIST, to the table and invite Ms Ryan to make an opening statement.

**Ms Ryan**—Thank you for the opportunity to discuss AIST's views on the proposed portability regulations.

**CHAIR**—You are always welcome.

**Ms Ryan**—The trustee members of AIST are in support of Senator Coonan's objective of assisting people to amalgamate small accounts. We understand the benefits that would accrue to members if they were able to do that more easily and if, indeed, they did do it. We also have no in-principle objection to improving portability arrangements. Given the stage of what you could call the evolution of superannuation legislation and regulation that we are at now, however, we believe that the regulations as drafted would not achieve the government's objective and, in fact, may undermine it by creating even more small accounts. In our view portability arrangements should be a part of the choice of fund environment, which of course we are not in yet, at least not in a mandated sense.

All of our reservations or qualification to various choice of fund proposals that have come before the Senate really can be repeated with this legislation. Again, we believe that consumers—that is, fund members—need protections against unscrupulous marketing. We believe that the cost of moving your money around, with exit fees in particular, need to be very well disclosed in very accessible terms so that members know when they join a fund exactly how much it will cost them should they wish to move money out of that fund. That is not the case as we speak. We are also concerned that the very favourable insurance arrangements that are available to many members of the public offer funds—industry funds in particular—cannot be extended to those members should they start moving their money about. Our other concern is that, given that the regulations as drafted do not restrict the frequency of transferring funds, we believe that there could be increasing cost subsidisation within funds from members who stay in the fund to members who take money out of the fund, and that that will create a whole lot of equity issues for trustee boards to have to consider.

We also would like senators to understand that we consider these proposals to be quite serious—not trivial in any way—and having the capacity to expose a lot of members of super funds to a level of risk, and we might even say danger, concerns us very much. This proposal would enable members to transfer virtually all of their lifetime's accumulation into another fund. If they are susceptible to unscrupulous marketing, they may choose a fund that is a very high-fee, low-earning fund. Through the publications of ASIC and the Australian Consumers Association last year, we know that there are a lot of high-fee funds which are low-return funds out there on the market. We would like to see more consideration of consumer protection, of

information and of the costs of such changes, and a better reflection of fairness and efficiency in the regulations before we could feel they would achieve their objective.

**CHAIR**—I have a couple of questions. Paul Watson from the MTAA made a very valid point in terms of portability, if we are not careful, having the potential to change established investment portfolios if there is too great a turnover. This could not only affect investment policy through their having a more liquid type investment strategy—although he did not use those words—but could also impact adversely if the churn rate was more than 25 per cent. Change could remove the very advantageous insurance arrangements that they have. Have your members looked at those sorts of issues?

**Ms Ryan**—We have looked at those issues. We are particularly concerned that trustees, especially in the current low return environment, are working very hard to find good long-term investment options. But many of those obviously reduce the liquidity of the fund; the most liquid investment you can make is cash and then it goes up from there. A lot of the infrastructure investments—which are proving to be good investments, although it takes quite a few years for the returns to come in—would be undermined if a fund had to keep 25 per cent or more of its accumulated funds liquid so that that money could be rolled out as members chose to roll their money out. Given the public policy purposes of superannuation, we think that is a very important consideration.

As I am sure you are aware, senators, the last couple of years have been quite difficult in superannuation, in that funds have had to report negative returns for the first time. This, of course, affects member confidence, and senators will be aware that the last APRA quarterly statistics, published a few days ago, showed that members' voluntary contributions are down. We believe that that is an unfortunate trend, because many people will need to make voluntary contributions to top up the nine per cent if they are to have an adequate retirement. And yet, in a climate of poor returns it is understandable, I suppose, that members are saying, 'We are not going to add anything to this.' In response to this drop in member contributions trustees really have to establish that they have got a good handle on long-term favourable investments, and members moving from one fund to another fund and then to another fund—I suppose 'too much churning' is the industry jargon for it—has to undermine that. We take that very seriously and our trustee members have discussed it a great deal.

**CHAIR**—Do you see a limited form of portability being possible?

**Ms Ryan**—We would support portability in conjunction with choice of fund where there was a higher level of consumer protection than there is at the moment. In our view, consumer protection goes to the way in which essential information is communicated to consumers—that is, that they understand clearly what it costs them to be in fund A and that they understand clearly, in dollar terms, what the fees are, including their administration fees, their investment management fees, exit fees and choice of investment strategy fees. We believe all of those fee disclosures need to be brought out in a much clearer way.

**CHAIR**—Do you think that we should make it obligatory for the receiving fund to provide a cost-benefit statement before they accept the moneys? For example, would it really be ethical for a superannuation fund to accept moneys out of a fund which was resulting in a 41 per cent exit

fee? We would be asking that new accepting fund to then refer it back to the member who had exercised that choice and ask, 'Do you still want us to proceed on this basis?'

**Ms Ryan**—I would be very much in favour of the receiving fund assuring themselves that the member actually knew what they were paying. There are still some very high exit fees in practice. One of our trustee members wanted me to bring to the committee's attention this situation: his son, who is in his 20s, had been working in different jobs, as young students and workers do, and he had a number of funds. His father said, as parents do, 'You should amalgamate all of those; you're paying all these separate fees.' I know it is a problem that the committee is very familiar with. The father identified a public offer industry fund that would be suitable, well run, with low fees. When he looked at his son's documents from his various funds, he realised that, in order for his son to leave one of the funds, which I probably should not name—it is a big commercial fund; a household name in this country—the exit fees were so prohibitive that the only way he could advise his son to amalgamate was to take all of his accounts from other funds which were in fact much cheaper and put them into the big, expensive fund.

Those high fees not only serve as an obstacle for people leaving but also they serve as a bit of a magnet for dragging small accounts in from funds which in other respects are better suited. So that high exit fee is really a problem. Senator Watson, should the regulations go through, I think there should be some requirement for a fund to say to the incoming member, 'Please sign that you know that this is going to cost you 40 per cent of your existing balance to move.' I think that would be an improvement.

**Senator BUCKLAND**—Following on from what you have been saying, can you give any indication at all, by way of a ballpark figure, of what it would cost to transfer all or part of the funds to another fund? I know it is a terribly hard thing to do because everyone has different fees. Is there a ballpark figure?

**Ms Ryan**—At the moment funds do charge different fees to their members for different activities but they are often subsidised. It is very hard to get to what it actually costs. I think it would be in the vicinity of a couple of hundred dollars. Ian, do you have any information?

**Mr Robertson**—We could ask.

**Ms Ryan**—You don't have transfers out of your fund because it is a public sector fund.

**Mr Robertson**—No, people are locked in.

**Ms Ryan**—The fund which I chair, the NRMA super plan, which is a big corporate fund, does not charge members for this. It is an old-fashioned, generous corporate fund. To this point most of the administration costs, including transfer costs, are absorbed by the company, the employers.

**Senator BUCKLAND**—It was not a very good question.

**Ms Ryan**—It is an important question. I am sorry I cannot give you a helpful answer.

**Senator BUCKLAND**—I think there is enough information from other inquiries for me to find that out if I really need to. If this were to be introduced and people could change funds and have portability, do you think there would be a revision by fund managers in that they would consider the introduction of an additional fee for those people who were fund hopping but who kept coming back to the first fund? If you dropped out because someone else is doing particularly well this year, so you go out for six months, get the big bucks and then say, ‘Hang on a minute, I’m getting nervous; I’m going back to where the compulsory contributions are,’ do you think there might be a danger that an additional fee could be introduced?

**Ms Ryan**—I think it is very likely that an additional fee would be introduced, because all of these movements create a cost. They also create an opportunity for the fund managers to develop a business. So I think undoubtedly we would see another layer of fees. We are very concerned about that because we are still very aware that, for the bulk of the work force, saving enough for retirement through superannuation is still a big challenge. Every time more fees are brought in, they eat into your savings. It is as basic as that. On the other hand, fees are a business opportunity to many in the industry, and they will be sought and applied.

We are dealing with a community environment where people are susceptible to proposals that are not necessarily in their interests, because of the low level of real understanding of how superannuation works and because of the poor disclosure of fees that we have had until now.

**Senator BUCKLAND**—I was interested in the comment you made earlier regarding the voluntary contributions being down. I think I heard that somewhere else. As someone who is uneducated in the field of superannuation—although I am learning—

**Ms Ryan**—I am sure you are, Senator, on this committee!

**Senator BUCKLAND**—It is likely to be because of the poor performance of funds that people are starting to think there might be a better way. I am just wondering if people are becoming more aware of the value of superannuation. A comment was made over a cup of coffee that people get that cheque—and it was referred to as the driveway analogy: you look at the cheque and think, ‘Struth, that is worth more than my car.’ Do you think people are becoming more aware? Do you think they do not understand the workings but they are becoming more aware of the total value?

**Ms Ryan**—I think they are. As people stay in superannuation longer and longer, their annual account balance report becomes a more substantial figure. Even though we have had a couple of difficult years, for someone who has been in superannuation for 10 years, since we have had the compulsory system, they are looking at an amount more than their car—in some cases, a lot more than their car, depending on what their earnings are. Members are becoming more aware, but of course the service provider sectors are becoming more aware too. When compulsory superannuation started, most people going into super for the first time had only a few thousand dollars and they were not of such interest to the commercial service providers; but now they might have \$100,000 or \$60,000 so they are starting to be of interest. I think awareness of the amount of money in superannuation is growing—on the part of individual members and the service provider commercial sector. Those two things create concerns for us.

**Senator BUCKLAND**—I am a creature of reaction and fear, I guess, but it put in my mind that people are starting to understand how much money they have in relation to superannuation, and they react quickly to rises and falls in performance. I guess that is a statement more than a question, but they are really reacting without an educated understanding of the long-term effect. They are performing badly at the moment. I know that my rollover fund did not go very well at all last year, but this year it looks like it is going to be vastly improved, from what I can pick up. I could have reacted and moved, but I think in the long term it will be better. The education thing is really starting to worry me.

**Ms Ryan**—I think your worries are well founded, Senator, I have to say. People got used to the idea that every year they would have a few thousand more than they did the year before—sometimes quite a few thousand more—and then suddenly they had less, the same or a few thousand less. And they say, ‘Well, I’ve got a lot of money here. This is my life savings in the making. Is there something better I can do?’

Senators will also be aware that alternative investment opportunities have been very heavily marketed to the community, particularly real estate—for example, city apartments and buying off the plan. In fact, some of the current affairs television programs have given some exposure to these practices. People are invited to seminars and told that you can put a small amount of money down as a deposit and this apartment block will return 50 per cent on your capital and so on, and people have lost money. Whereas they might lose a few thousand in a bad year in superannuation off their total accumulation, which has been growing, they will lose a lot if they tie themselves up with a real estate deal that goes badly. So I do think there are dangers in making it too easy to shift your money around without having the knowledge. The AIST is an organisation devoted to education and we do say at every Senate hearing and on every possible occasion that we do think there needs to be much more public education about super.

**Senator BUCKLAND**—It is interesting reading through the submission and there is a fairly common chord, which leads me to believe that we have a lot more to do before people like me will be comfortable with our knowledge of superannuation. I think I would probably represent the bulk of Australians with my knowledge.

**Senator CHERRY**—I have a small number of questions. Coming back to the issue of fees and charges—and Senator Watson and I were just discussing this privately—how would you actually implement a change to exit fees to restrict them to, for example, the costs of processing, as you have suggested? That could almost be only prospective on your contracts, couldn’t it?

**Ms Ryan**—I think you are right. I do not think in superannuation we can change anything retrospectively—unfortunately, some people might say. So as to those high exit fees that are in place where a person has contracted to go into a fund that has high exit fees, I do not think legislatively you would want to try to change that. But, going forward, there could be some mandated prescription that fees shall be no more than X per cent of the amount. I am thinking of when parliament brought in the member protection arrangements, for example. There was an arbitrary amount and a requirement that that amount be protected. I think it would be open to the parliament to make a regulation going forward that would limit that.

The other thing you could do legislatively—and I hope you will—is require that, henceforth, all exit fees be expressed in dollar terms and that some process be mandated. Senator Watson

was suggesting one for the receiving fund, but I think you could also have a process for the fund which was losing the member—some process where the trustees of that fund have to satisfy themselves that the fund member knows how much in dollar terms it is going to cost. I think we all hope that, in the competitive environment that we do have to a large extent in super, forcing realistic disclosure of fees might also bring about a voluntary reform of those fees, because if people know what it is going to cost them—

**CHAIR**—We should shame them into it, shouldn't we!

**Ms Ryan**—That is where I was heading.

**CHAIR**—And they should show just cause as to why they are charging 91 per cent or whatever. That would soon change the culture of some of these companies.

**Ms Ryan**—Yes, that is right—you could expose them, name them in parliament and those sorts of things, and put a bit of commercial pressure on them.

**Senator CHERRY**—And put them in stocks in the main market square and a few things like that!

**Ms Ryan**—That kind of thing.

**CHAIR**—They are unconscionable, some of these fees.

**Ms Ryan**—There is the problem that they are already in place and I do not see that they can be unwound for the people who have already made those arrangements, but they can be exposed. It may be that a provider that charges these high fees might themselves review their fees. In this new climate of choice of funds and portability, which, I guess, will be in one of these days, they might modify their fees. The company charging the fees can decide to do it retrospectively.

**CHAIR**—If you introduce a concept of portability you may, as the previous witnesses suggested, inadvertently move more and more funds back to a situation of charging higher fees for exit just to protect their state in the market. We have to try to foresee all possibilities, don't we? How realistic would that be?

**Ms Ryan**—I think the funds whose trustees are members of our organisation would be reluctant to do that because we have been great critics of high fees, as you would be aware.

**CHAIR**—If we see churning increasing how do you protect your existing base?

**Ms Ryan**—Without speaking for my colleagues, I would think that if we on the trust board of the NRMA fund, for example, saw this churning going on and absorbing funds either from the company or from the fund, as trustees we would have to look at imposing a higher fee because the whole of the fund is being affected by the cost of administration, churning, the money going out, the loss of long-term investment strategies and so on. It is a problem.

**Senator CHERRY**—I had a related question about partial transfers. You indicated in your submission that members should be permitted to request only one partial transfer a year. Is that a fallback position? What is your view generally on whether there should be partial transfers?

**Ms Ryan**—I suppose our view is that we would like these regulations to be deferred until we have a coherent choice of fund environment. If this does not happen, if the Senate decides in any event to pass the regulations, then we would like that once a year because it seems that that does give people a reasonable choice but would stop the churning and the costly administrative processes. It would also, I hope, encourage the member to think carefully about the change. If you had a situation where you could go onto the Internet and switch your money out every week, some people would do that as they do in the United States with their choice of investments. They change them daily. We have nightmares at the thought of that happening in our funds in Australia. It is an arbitrary figure; it is a fallback.

**CHAIR**—We do not want to go down that track because those sorts of funds are, essentially, locked into equities. We really want some super funds to be in long-term structural infrastructure, don't we? We do not want to change the whole nature of sound investment strategy just to meet a concept.

**Ms Ryan**—I think that is correct. Superannuation is different from just playing the stock market. Government has established superannuation and gives it tax benefits and a regulatory structure and so on for a purpose and the purpose is that people's savings will be more protected for their retirement.

**CHAIR**—And there is diversified investment.

**Ms Ryan**—That is right. We discussed it amongst ourselves and we thought a year is reasonable. Anything more frequent than a year could lead to fragmentation, churning and costs.

**Senator CHERRY**—The other issues I was seeking to address were largely dealt with by others—liquidity and multiple accounts. Is there any comment you wish to make at this stage about how this will lead to the proliferation of accounts, which is an assertion several people have made?

**Ms Ryan**—The example would be that somebody is in a public offer fund where portability could apply, not in Ian Robertson's fund which is a public sector fund—and that is another big problem. We are talking about portability and rationalisation, but we still have this huge roadblock where you cannot transfer between your public and private sector funds. We are not here today to give you a prescription as to how that must happen, but I think it should be in the minds of all public policy designers that that is still something that needs to be dealt with. I know it involves the state governments and so forth.

But say you are in my fund, the NRMA fund. When this comes in, you may see some marketing and say, 'Oh well, I'll take a third of my money out and put it in this new fund that looks so fantastic.' You are susceptible to this sort of marketing, so then when someone else comes along and says they have a great fund, you may say, 'I'll take half of what is remaining and I'll put it over there.' I will keep taking bits out of my basic NRMA super plan to try to get advantages that I am told exist in these other funds. So instead of just having my one

superannuation balance, in my NRMA fund, I have now got three or four. That is how we see it playing out. Some people will be susceptible to the marketing—and the marketing will occur. We have no doubt of that, because there is a lot of money involved, a lot of business to be made.

**CHAIR**—There being no further questions, thank you very much.

**Ms Ryan**—Thank you for the opportunity.

**CHAIR**—The issues in this inquiry are fairly succinct, aren't they?

**Ms Ryan**—I think you will find a high degree of agreement from those of us who are focused on members. Thank you very much.

[11.17 a.m.]

**BLOCH, Ms Jo-Anne, Deputy Chief Executive Officer, Investment and Financial Services Association Ltd**

**GILBERT, Mr Richard, Chief Executive Officer, Investment and Financial Services Association Ltd**

**STANHOPE, Mr Bill, Senior Policy Manager, Investment and Financial Services Association Ltd**

**CHAIR**—Welcome. We invite you to make an opening statement.

**Mr Gilbert**—Thank you, Mr Chairman. We would like to make an opening statement and give evidence today. We would also like to make the point that we appreciated very much the report that this committee produced yesterday or the day before on retirement income streams. We particularly congratulate the committee on recommending that the government look closely at further opportunities for retirees in the form of growth pensions, so we come to this committee very enthusiastically today to speak about this particular topic as well.

**CHAIR**—It is all complying pensions that we want to encourage, including growth pensions.

**Mr Gilbert**—That is right, with the flexibility that that provides.

**CHAIR**—Yes, to make them more attractive.

**Mr Gilbert**—Yes, I take your point. I think the flexibility that provides will be good for the Australian community. Turning to portability, we support the portability of superannuation benefits as a key consumer sovereignty issue. We stress that consumer sovereignty should be at the heart of these sorts of decisions. ‘Consumer sovereignty’ is a complex term and a complex concept. It includes taking into account such things as the right of consumers to select where their money should be in terms of returns, where their money should be in terms of fees and where their money should be in terms of the entity which is managing those moneys and the entities managing the moneys underneath. While ‘consumer sovereignty’ is a complex term, nevertheless it is something which should be paramount in regulating superannuation in Australia. We believe that portability can proceed on its own. It does not need to be proceeded with or followed by choice—it can proceed on its own; it is a separate thing—and the regulations which have been put in place will work to do that. We are proud of the fact that our industry has portability. There is scarcely a fund in our industry—or out in the retail sector, at least—which would deny an individual the right to have portability in moving funds. That is our opening gambit. We would be very happy to take questions.

**CHAIR**—You say that there would hardly be a fund that would deny portability. But if funds have very high exit fees, surely that is a denial of portability. How many of your members would have portability fees that would be substantially in excess of the administrative costs, plus a small profit, associated with the exit?

**Ms Bloch**—I think you will find that you are talking about the existence of products that were written in the mid-1980s and were associated with life companies and superannuation written through life companies. Those sorts of contracts were written on the basis that the cost structure was amortised over the period of the contract, which in many cases was 20 or 30 years. That element is only about five per cent of funds under management, and probably only about two per cent of the membership that we would be talking about. The contracts at the time were written on the basis that the person who went into the contract would have that contract for the term of the contract. If they keep the product for that term, those sorts of exit fees do not actually apply. The problem occurs if they try to get out of the contract early in the term.

The industry has worked hard to change the nature and the structure. If you would recall, in the mid-1980s there were a lot of incentives around tax deduction and so forth—in fact, the whole market has changed quite considerably. So what we find is that the majority of our retail clients are now in a structure where the exit fee is possibly no more than five per cent, and in most cases actually drops down to zero—except for a dollar based administration type exit fee of \$30 or \$40—on the basis that there is a different fee structure. So I think you will find that the majority of clients are actually in products that have very reasonable exit fees, if at all.

**CHAIR**—Ethically, though, if you have a contract that was written in the early 1980s when there were other tax arrangements around that encouraged those sorts of high exit fees, surely we should have a mechanism to culturally change that attitude. I just cannot see, 20 years later, an exit fee of 91 per cent, as we had quoted this morning, being valid. Surely most of those costs would have been recouped in the 20 years, and for there still to be a 91 per cent exit fee does not seem to be ethically justifiable.

**Ms Bloch**—Can I say that that exit fee would only be applied if that person actually left. The whole idea of the contract and the benefit of the contract is to stay there for the term of the contract. It was written on the basis that the fee in the first place was much lower and was spread across the life of the contract. So from a client's perspective, an investor or a superannuant's perspective, the structure would have benefited them earlier in the piece, and therefore will benefit them if they stay for the term of the contract.

**CHAIR**—I put it to you that a submission was given to this committee that those companies or institutions that have high exit fees in terms of portability would tend to be the ones that people would move to because they could not afford to move out of them. Surely we do not want an environment built on that sort of logic.

**Mr Gilbert**—Our view would be that these regulations provide for adequate protection for the consumers in that they have the opportunity to find out what the exit charges are. I would also put to you that under the financial services reforms, if a financial planner moves down that track and triggers for an individual those sorts of charges, I do not think that financial planner would have their dealer's licence for much longer. I would be very interested to find out whether that claim has been substantiated. I have not seen the particular evidence, and so until we see that evidence and have a chance to respond—

**CHAIR**—Of the 91 per cent or the 41 per cent exit fee?

**Mr Gilbert**—I would like to see the policy and the consumer's letters to the company and back. Really, for us to publicly talk about a specific case which could then be inferred to be a generality, I think would be very dangerous.

**CHAIR**—We will try and get that. You can see the situation that we are worried about. If you have a very high exit fee, people will be told there is no point in transferring your existing employer arrangements because the cost is too high. On the other hand, if you have six other accounts, it would probably be far better to amalgamate those with the high exit account. Because it is too costly to get out, you might as well stay in and build it up.

**Mr Gilbert**—Possibly.

**CHAIR**—I have been talking about trying to anticipate what consumer behaviour is going to be in an environment of portability.

**Mr Gilbert**—What is important about these regulations is that they are not regulations designed so that consumers must do things; consumers may act to have a portable decision. We do not expect that this is going to lead to a very high turnover between funds. This is going to be measured. It has an overlay of disclosure on top of it. The other thing I would like to put to the committee is that this is part of a package of reforms which should prevent those sorts of products being offered to people in the future. Many people offered those products with high exit fees never had a choice about where that money went. The employer was sending that money to a fund, or a life insurance company in most cases, and the individual never had a right to be able to move that money elsewhere. This is an opportunity to give individuals some sovereignty over where their assets go and to prevent them being put into products which are absolutely incompatible with their needs.

**CHAIR**—We are saying that this right may come with an enormous cost. I admit that with the new generation of funds the cost is unrealistic, but we are still grappling with a lot of cases of high exit fees.

**Ms Bloch**—This is really confined to a very small percentage of the retail population. In many cases, companies have offered alternative arrangements and have tried to work with those individuals and their advisers on different sorts of arrangements. In fact, a lot of these products also have a lot of benefits, such as life insurance and all sorts of other things with them. To look at these products in terms of the exit alone is actually missing a lot of the value of some of these products. Having said that, they are no longer offered; they are closed, and it is a declining population.

**CHAIR**—It has been suggested that portability could be choiced through the backdoor and that without accompanying legislation we could have a siphoning off and consequent problems for the employer contributing to a fund which an employee wants to exit through portability. There is no legislative support as there would be under choice.

**Mr Gilbert**—We would draw a distinction between the two mechanisms. Again, the only similarity between choice and portability is that both of them have a very large element of consumer sovereignty. It is interesting to read the media because it talks about funds which might have high costs. If that is the case and there are funds with high costs, individuals should

be able to elect to put their money where there are low costs, where there is an investment strategy which is appropriate to their needs, or indeed where there is trusteeship or custodianship of those funds which meets their needs. They are the elements of what we call consumer sovereignty. Portability delivers that and choice delivers that too, but these two measures can run independently.

**Senator BUCKLAND**—Don't you think achieving a high degree of consumer sovereignty could translate into a high degree of consumer risk as well?

**Mr Gilbert**—We have consumer sovereignty in a whole host of economic activities in this country. One of the interesting parallels is in university education, for example. An individual makes a choice about their university and pays a HECS tax—it is a compulsory tax.

**CHAIR**—It is a compulsory price for education, is it not?

**Mr Gilbert**—As is super to some extent because of the SG. The individual makes a choice about their university and their faculty and that choice could make or break them career-wise. We allow them to do that; we do not allow them to do that for superannuation. We find it hard that superannuation is perhaps the only product where you do not have the right of consumer sovereignty.

**Senator BUCKLAND**—I am not sure that I could agree with that analogy. Be that as it may, it is one that we should take into consideration. I just wonder what will happen if portability as you are suggesting were introduced without an effective education campaign. This has been spoken about for a long time. There is concern among some of us that people are not sufficiently educated to take advantage of what you term 'consumer sovereignty'. I have the real fear that portability, if it were introduced and supported on the grounds that you are supporting it, without an education program first being introduced and having had time to take effect, would mean that consumer sovereignty could only be taken to mean consumer risk. I have a very real fear of that.

**Mr Gilbert**—Fifty per cent of individuals now coming into an employer are choosing their superannuation fund. One hundred per cent of individuals are choosing the destiny of their lump sums when they retire. We have just experienced perhaps the worst financial markets that we have had probably since the Depression and, interestingly, we have not had large-scale or even significant market failure in terms of the choices individuals have made for their retirement products. Ms Bloch might want to add something to that.

**Ms Bloch**—I think we do agree that education is important, but I concur that choice is out there. We have mentioned that our retail members provide portability already. I think that there is quite a lot of education that is there already, but I do not think we would disagree that education is important.

**CHAIR**—Just to help Senator Buckland a little bit, I think he makes a valid point. He used a very good analogy in relation to education. The only thing is that that is not mandatory, whereas superannuation is. I would like to add that to his comment. We are imposing something on something. We are not imposing a dentistry degree or an architecture degree on your son or your daughter, with all the costs associated with that, whereas superannuation is a mandated product. Because it is a mandated product, I think there is a higher element of need for parliamentarians

to ensure that there is a reasonable element of consumer protection associated with that implementation.

**Mr Gilbert**—I would not disagree with that. We believe that the way to do that is through the disclosure regime. We have just passed perhaps the most impressive and far-reaching disclosure regime on this industry that has been passed yet and we should have faith in that regime.

**CHAIR**—I am sorry, Senator Buckland. I just thought I would add that.

**Senator BUCKLAND**—Thanks for that. It was very valid. Earlier on I asked a witness about fees and whether fund-hopping—and that is my term—to try and get the best buck for your investment might encourage funds and fund managers to introduce new fees, particularly in the areas where the principal amount—that is, the compulsory amount—is with one fund but then your other contributions can be transferred between funds if you keep coming back to the original fund every now and again for a little bit of a rest period. Would this encourage funds to increase their fees or introduce new fees?

**Mr Gilbert**—This industry presently is very fee sensitive. The community is very fee sensitive. Any provider putting fees up in this environment would not be in the market all that long. There is very strong downward pressure on fees and there is going to be a lot more.

**Senator BUCKLAND**—In your consumer protection measures in your submission you talk about how IFSA has been active in developing uniform and effective fee disclosure measures. Reading that, I am not too sure. Has that finished? Has the process finished?

**Mr Gilbert**—We hope that on Monday or early next week the regulator, ASIC, will be releasing that uniform model so that consumers, regardless of which fund they are in, will actually have access to a comparable fee statement.

**Senator BUCKLAND**—So it is only a hope that that will be the case. People do not necessarily have to disclose.

**Mr Gilbert**—Under the FSR all fees have to be disclosed. This statement makes funds, regardless of what segment they are in, disclose them in a similar way—on one sheet of paper, basically. I think that is a very positive development. This is long-awaited. This committee drove disclosure in the sense of all fees—

**CHAIR**—That was our recommendation as a committee to ASIC.

**Mr Gilbert**—in its second and third reports in the early nineties. This is, I believe, the icing on the cake and it is very important that we get this right.

**CHAIR**—You were probably secretary in those days, Mr Gilbert.

**Mr Gilbert**—That is correct.

**Senator CHERRY**—I have only one question. I was looking at your submission relating to the current portability provisions. Could you expand on what you see as the impediments in the current provisions to portability?

**Mr Stanhope**—Do you mean in our sector or generally?

**Senator CHERRY**—Generally, in terms of the SIS regulations and also in your sector.

**Mr Stanhope**—Principally, because superannuation began as an employer-sponsored arrangement, outside the retail sector of course, the typical requirement has been for a SIS trigger event, usually leaving the employer through resignation, retrenchment or retirement. So fund rules tended to be built around those. In some cases in our sector, corporate master trusts still have that kind of arrangement, whether it is because employers prefer it or because it is part of the pricing structure of the fund. The major direct barrier to portability is a fund rule that says you have to satisfy a SIS trigger event—that is, to be able to have a rollover.

For most of the funds offered by our members, certainly for the retail superannuation funds offered to individuals, there are no barriers to portability that we are aware of. If you ask your fund to roll over your amount, including parts of your amount, generally speaking they will do that. The only limitation there is that, at the bottom end where the fund may have minimum balance requirements and where your remaining balance falls foul of that, the fund may close your account. In fact, we suggested to Treasury in that case that the trustee would be best sending the whole dollar value of the rollover to the chosen destination account rather than sending an orphan amount to an ERF. In the corporate retail master trusts segment that our members offer, there are still some funds that require SIS trigger events, but, as far as we can tell, the majority of those funds in practice will still allow portability if the member requests it.

**Senator CHERRY**—So essentially, in terms of your sector, excluding those funds that are restricted by the SIS trigger events rule, this regulation does not really impact on your sector at all?

**Mr Stanhope**—No. We are already doing what the regulations would require.

**CHAIR**—If we are not restricting it to one decision a year, could the portability lead to a change in the investment structure? For example, if you were a trustee on an investment committee, it would not be hard to envisage being concerned about limiting or reducing the proportion of your investment in infrastructure, which I think is always a good investment for super funds, and placing it more into equities along the lines of the US funds, which are heavily locked into equities. Given the current government's encouragement for infrastructure arrangements to go more and more into the private sector, these do seem to be good vehicles. If you had too much portability, wouldn't a behavioural consequence by trustees be: 'We've got to exercise a degree of caution and limit our exposure to that particular market'? That would worry me.

**Mr Gilbert**—I would like to answer that in two parts, if I may. Mr Stanhope could perhaps talk on the technical provisions and then I would like to speak about the macro and microeconomic effects.

**Mr Stanhope**—The regulations, which were actually made yesterday, have a limitation—at regulation 6.35(1)(c)—limiting the requirement that a trustee roll over money where a member has requested a rollover in the previous 12 months. So this provision effectively requires trustees to roll over only once per 12 months.

**CHAIR**—Are there any other significant changes that came in yesterday?

**Mr Stanhope**—Treasury released their draft regulations for comment some time ago, and that was a comment that IFSA and a number of other organisations had made, that they would prefer to see a mandatory rollover apply only once every 12 months. That is in the regulations at the point that I have referred to.

**CHAIR**—And they have now introduced that?

**Mr Stanhope**—Yes. I guess the second thing to say, on that side, is that most accumulation funds—aside from the infrastructure issues, which Mr Gilbert will comment on—are priced daily. The whole culture of the Australian industry, as you know, is a daily ‘mark to market’ culture, so it is not particularly difficult to transfer amounts when a member wishes, depending on the fund that they are in.

**Mr Gilbert**—So I guess our point on the impact on infrastructure investment—possibly—is that ultimately that is a decision of the trustees: to make the right call about what strategy they are going to have in place to ensure that that fund has the right return, risk and liquidity elements in it. We have had a steady move to choice. As I said earlier, 50 per cent of employees are now choosing their fund. That in itself causes fund flows to wax and wane for various funds, and trustees have very successfully dealt with that environment, which is more fluid and less certain than they would have had, say, 10 years ago.

In relation to infrastructure and unlisted investments, a superannuation trustee who invests overly in infrastructure, unlisted, does so at a risk to its members and could force itself, if it did not get the right structure, to sell those assets off at a value less than would be the market value. What I think is important here is that trustees have to get that decision right. Clearly, infrastructure assets are listed on the Australian Stock Exchange, have a daily price and can be redeemed overnight. So I do not see that there is any danger to infrastructure investments as a consequence of portability. I think that borders on being a red herring.

**CHAIR**—Thank you very much. We notice portability will apply to accumulation of funds and members of fully funded defined benefit funds who have left employment with an employer sponsor of such a fund. It will not apply to unfunded public sector or self-managed funds, or to benefits being paid as a pension. So portability, under the regulations issued yesterday, still will not apply to defined benefits if the person is currently in employment?

**Mr Gilbert**—Yes.

**CHAIR**—Whereas, under choice, it did—that was one of the problems which the committee had with the previous choice rules.

**Mr Gilbert**—We accept those restrictions. I think one of the difficult experiences we have had in this consumer sovereignty debate is people alluding to the Australian situation versus other jurisdictions where there have been more aggressive incursions into consumer sovereignty, which have—as I think Senator Buckland was alluding to indirectly—led to some problems for consumers. I think our moves here have been measured, that this package is a measured package, and that is why we support it.

**CHAIR**—So you think it can proceed without the accompanying package of choice legislation?

**Mr Gilbert**—Portability can proceed alone. It is sufficiently well quarantined—and, I think, packaged—to allow it to do that.

**CHAIR**—There being no further questions, that is probably a good positive point to finish on, Mr Gilbert. Thank you.

**Mr Gilbert**—Thank you very much.

[11.48 a.m.]

**FRASER, Mr Garry Robert, Principal, Watson Wyatt Australia Pty Ltd**

**JEFFREY, Mr Bradford Mark, Head, Superannuation Consulting (Sydney), Watson Wyatt Australia Pty Ltd**

**STANHOPE, Mr Bill, Senior Policy Manager, Investment and Financial Services Association Ltd**

**CHAIR**—Welcome. Do you have any comments to make on the capacity in which you appear?

**Mr Jeffrey**—I am head of the superannuation consulting practice in Watson Wyatt's Sydney office.

**Mr Fraser**—I am a principal for Watson Wyatt in its Sydney office.

**CHAIR**—I invite you to make an opening statement.

**Mr Jeffrey**—We are very pleased to address the Senate Select Committee on Superannuation on the draft portability regulations. Watson Wyatt is a superannuation and actuarial consulting firm and has been in existence in Australia for over 20 years. We work with a large range of corporate superannuation funds, advising them on all aspects of actuarial and superannuation consulting matters as well as administration. Our overriding concern with the draft portability regulations is that they, effectively, introduce choice of fund before the primary choice of fund legislation has been passed. We believe it is inappropriate for these regulations to be passed before the choice of fund legislation is passed. Further, these regulations are more extensive than the choice of fund proposals, as they apply to a member's total accrued benefits, not just benefits produced by future superannuation contributions. We believe the regulations should be consistent with and follow from the choice of funds legislation, rather than being in advance.

In terms of our specific concerns, our submission addressed seven areas. The first two related to defined benefits, and the difficulties with defined benefits in terms of the portability regulations as we had them on 15 July.

**CHAIR**—They are excluded, though, aren't they?

**Mr Jeffrey**—In the regulations on 15 July, contributory defined benefit arrangements were excluded, but not non-contributory defined benefit arrangements.

**CHAIR**—One of our difficulties is that the new regulations just came out yesterday, so neither the witnesses nor I have had an opportunity of looking at them.

**Mr Jeffrey**—We just heard your reference to that while we were sitting in the audience. If they are totally excluded then we are totally in support of that, because—

**CHAIR**—Can you just check on that for us straight away? We might ask some of the previous witnesses in the audience to clarify this issue for us.

**Mr Stanhope**—A defined benefit interest in a defined benefit fund is excluded.

**Mr Jeffrey**—For a standard employer-sponsored member?

**Mr Stanhope**—Yes.

**CHAIR**—That might help you.

**Mr Jeffrey**—Then we are in support of that. I will not waste the committee's time by going through the reasons for that.

**CHAIR**—That is why I sought that advice.

**Mr Jeffrey**—The third area that we are concerned with is costs. Allowing partial transfers or withdrawal of benefits at any time will, we believe, increase fund costs due to items such as additional benefit processing, additional surcharge reporting and investment costs. Clearly, the legislation needs to make it clear that such costs should be equitably allocated to the members who make use of this facility.

The fourth area is surcharge. The portability regulations will place additional pressure on existing administration systems to cope with surcharge reporting. I am sure the committee is well aware that surcharge reporting has been a very onerous and complex task undertaken by superannuation funds. Much has been invested in administration systems to deal with the current level of surcharge reporting and that will need to be clearly amended and enhanced due to the ability to take out partial transfers. In our submission we cited examples where this will cause additional reporting requirements.

The fifth area is in relation to insurance cover and the potential loss of insurance cover by members. Often, insurance cover is purchased through a deduction from a member's account. A member could inadvertently take out all of the money in their account, leaving insufficient or zero funds in there to cover deductions for insurance premiums, meaning that their insurance cover would cease. A way of guarding against that possibility would be to give trustees the ability to withhold funds to cover at least a certain period of insurance premium deductions, but that would in itself mean more administration.

The sixth area is the potential for increased churning where people are encouraged to transfer accrued superannuation entitlements from one fund to the next. That could potentially lead to more rather than less member superannuation accounts. The final area relates to the ability or need to adjust benefits because of complications that will arise when members are able to take out partial withdrawals. An example that we cited is where a death benefit was a fixed multiple of salary—say, four times salary. The insurance component of that would be the difference between the four times salary and the member's account. If the member's account was withdrawn, the insurance cover would need to increase. If that was being financed by an employer contribution, it would put an increased contribution cost on the employer. Alternatively, the employer would need to be able to reduce the level of cover by the amount of

money withdrawn. They are the seven areas that are covered with specific examples in our submission.

**CHAIR**—Thank you. You have raised very significant issues. You come to us essentially as an administrator of superannuation funds?

**Mr Jeffrey**—We provide both administration and consulting services to superannuation funds.

**CHAIR**—Say I have recently left an employer, I have some surcharge obligations going back two or three years and I elect to consolidate my superannuation account using the portability rules, is there any requirement to notify the tax office that I have moved to a different fund? How is the tax office going to chase a fund with a surcharge debt?

**Mr Jeffrey**—Chasing it is a difficult issue at present, with surcharge reporting. If we are not the holder of contributions at the time a surcharge assessment is received, it is our obligation to tell the tax office where the member has transferred to so they can start chasing it. If a partial withdrawal is taken and we have to report surchargeable contributions, a difficulty will be how much of the surchargeable contributions for that year relate to the partial withdrawal. The partial withdrawal could be in relation to a number of years of benefits. So there will need to be some way of apportioning surcharge contributions or determining whether they should be reported as moneys that have been transferred to another fund.

**CHAIR**—So the tax office could be a couple of years behind and, in that time, somebody could have made a transfer through portability on at least two occasions?

**Mr Jeffrey**—Absolutely.

**CHAIR**—If there is a surchargeable debt and somebody wishes to transfer their superannuation entitlement to another fund, is there an obligation on the administrator to notify the tax office?

**Mr Jeffrey**—The obligation exists when we receive the surcharge assessment from the tax office if they are not currently a member of our fund.

**CHAIR**—If they have not received a taxation assessment but, in the nature of things, you know that there is an assessment to be received, how does that affect your reporting obligations to the tax office?

**Mr Jeffrey**—It does not, because we do not know that there is a surcharge assessment to be received. That will be determined by the person's taxable income, which we do not have any information about. As an administrator, we can only react to assessments received by the tax office.

**CHAIR**—The tax office will send you a notice. You reply to them and say, 'We've no such account for a person.'

**Mr Jeffrey**—Correct. We transfer that account to XYZ, and they have to go and chase it up with XYZ. That person could have moved on from XYZ to ABC. It could take years and years, even under the current regime, to track down. I think that will only be enhanced by partial withdrawal.

**CHAIR**—That is an issue that we might have to ask the Taxation Office to look at.

**Mr Jeffrey**—Further reporting requirements or adjustments to administration systems will be needed under these proposals, and the industry will need some time to amend administration systems.

**CHAIR**—For the surcharge or for other issues as well?

**Mr Jeffrey**—The surcharge is the primary one that will complicate the administration.

**Senator BUCKLAND**—You mentioned that there may not be enough funds left in the exited fund to pay the costs. If funds were held in the original fund to pay the fees, the funds that were held would still attract administration fees, wouldn't they?

**Mr Jeffrey**—Yes, they would. If you have an account, you will be charged an administration fee.

**Senator BUCKLAND**—So you will be paying administration fees for money that is sitting there only to pay fees. Is that right?

**Mr Jeffrey**—You would be paying administration fees if you had an open account and that account was receiving contributions.

**CHAIR**—The problem of non-contributor defined benefits has now been removed. The costs one is still there, the surcharge one is acknowledged to be causing additional pressure and also there is an insurance one. Do you think trail commissions should be associated with mandated superannuation?

**Mr Jeffrey**—We are not charged trail commissions.

**CHAIR**—I am just looking at item 6 of your submission, which deals with churning. Increasingly, the better financial advisers are moving to up-front fees. But if somebody says to an employee, 'It won't cost you anything because there is a trail commission,' then surely there is a greater likelihood in a behavioural sense for there to be an increase in churning?

**Mr Jeffrey**—That is correct. I think that applies under the existing choice of fund proposals and portability. They are basically one and the same.

**CHAIR**—Do you really think that disclosure alone will counter the impact on churning?

**Mr Jeffrey**—No, I do not. It is human nature. We may disclose things. We have not had the full disclosure regime of FSR as yet, but there is enhanced disclosure and that is a good thing. Whether people will understand or appreciate full disclosure is another matter.

**CHAIR**—You are a worldwide organisation. Can you speak from your experience in relation to these issues overseas?

**Mr Jeffrey**—Only in a general sense. We are in the United Kingdom. Our UK colleagues have witnessed the pensions mis-selling events in the UK. All I know is that it has been a serious and material issue. I have seen, as I am sure have others, figures quoted of mis-selling requiring 11 billion pounds of compensation. But I know about that only in a general sense. I would be pleased to make further inquiries to our UK office, if you would like further information, and to give feedback to the committee.

**CHAIR**—We do not want to destroy some of the unique, very good features of the Australian system that we have built up over the years. We do not want to inadvertently let them slip without putting in some sort of protective measure. This committee has a strong focus on consumer protection. We want to maintain that. It is always a worry to have changes in behaviour. We do not know what the consequences of our well-intended legislation might be. It could well be that it changes consumer patterns in a way that we might not think is a good idea in the long term.

**Senator BUCKLAND**—I was going to ask you about the effects of introducing portability without choice. As consultants, how do you view that?

**Mr Jeffrey**—I think if you introduce portability without choice you have actually introduced choice, but you have introduced choice in a less efficient fashion. You can effectively achieve the same end under portability as you would achieve under choice by accruing a benefit and then transferring it out, and again accruing a benefit and then transferring it out. You could accrue a benefit for one month, transfer it out at the end of the month and accrue a benefit. So effectively you have choice with just a one-month lag, but you have much more cost because you are continually having to move money from fund to fund rather than having it directed straight to a fund.

**CHAIR**—You can exercise it once under yesterday's rules—it would be diminished, would it not?

**Mr Jeffrey**—Once in total or once a year?

**CHAIR**—Once a year, I thought.

**Senator BUCKLAND**—Yes, once a year.

**Mr Jeffrey**—I apologise for not knowing about these latest regulations, but I think it is a sensible move. I recognise that it reduces the flexibility of choice, but you have got a tension there between full flexibility and addressing the behavioural issues you referred to before. So it sounds sensible to put on a cap of once a year. But still you have got choice. It is one year, but then every one year you roll over money. You still have fund choice, just with a slightly longer lag than I referred to before. That is why we think it is inappropriate for them not to be linked—they are inextricably linked and they should be considered as such.

**Senator BUCKLAND**—Overall, your submission is suggesting that this move would give an overall cost to the consumer anyway. That is the thrust of your submission. Have you done any modelling at all, or been able to do any modelling?

**Mr Jeffrey**—We have not done any modelling. But we know that it will produce extra work—therefore there must be a cost associated with that. In some instances, that extra work may need to be manual rather than automatic, which only exacerbates that situation.

**Senator BUCKLAND**—The only other thing I was going to ask you was whether you are familiar with automatic consolidation.

**Mr Jeffrey**—I am not sure what you mean, sorry. Making it compulsory to automatically consolidate previous accounts?

**Senator BUCKLAND**—I am not familiar enough with the term myself. I was hoping someone was going to be able to enlighten me, but I will not pursue that.

**CHAIR**—It is always good to hear from administrators who have to handle these legislative changes. AAS are appearing this afternoon, who are also raising this issue of the surcharge. That is a big issue, and we have got to be careful how we handle that.

**Mr Jeffrey**—It is enormous from an administrator's perspective. Seeing it from our end, with how difficult it has been to administer the surcharge, to add something which will complicate that already complicated administration fills us with some trepidation.

**CHAIR**—Thank you very much for appearing before the committee. We really endeavoured to get a wide range of input, and having administrators appear before the committee is very important. We will certainly take your views into account. I apologise for the inconvenience of conducting an inquiry while regulations are coming out which could impact on your submission.

**Mr Jeffrey**—Thank you for the opportunity.

**Proceedings suspended from 12.08 p.m. to 2.02 p.m.**

**CARPENDALE, Mr John Joseph, Deputy Chief Executive Officer, Queensland Local Government Superannuation Board (LG Super)**

**SMITH, Mr Peter James, Chief Executive Officer, Queensland Local Government Superannuation Board (LG Super)**

**CHAIR**—Welcome and thank you for coming—we appreciate you making the journey and taking the time to make a submission. We must first apologise because this morning we were notified that yesterday afternoon the Treasury issued some further amendments to the regulations on which everybody has based their submissions. This could be something of an embarrassment because the full extent of your submission may well be changed as result of what Treasury has put forward. I think it is incumbent upon me to read this statement to you before you make your presentation:

The Government's revised Portability Regulations were gazetted this morning, together with accompanying Explanatory Statements. I wish to note that the final regulations include a number of revisions to the draft regulations from which we have been working. In particular, the SIS Amended Regulations 2003 include three major revisions:

1) Revised disclosure requirements: Regulation 6.34(2), introduces new requirements relating to disclosure of fees and charges by trustees, and the impact of a transfer on a benefit statement.

In appearance that seems to be a good move but we would naturally be interested in hearing people's reactions to these revisions. The statement continues:

2) Partial transfers out of the account: Regulation 6.35(1)(b) provides that a trustee of a fund may refuse a request for a transfer where the fund will hold less than \$5,000 following the transfer.

3) Transfers out of an active account—

that is, the account into which the employer is paying—

Regulation 6.35(1)(c) provides that a trustee of a fund may refuse a request for a transfer where a transfer has already occurred in the last 12 months.

The committee will invite parties to make supplementary submissions on these issues.

We apologise, but it was outside our control. The government put us under a very tight reporting mechanism and we proceeded with that, not knowing that there were further regulations in the wind. We invite you to make your submission and acknowledge that you have been faced with a degree of difficulty because some of these issues were referred to in your submission.

**Mr Smith**—Thank you. I will say at the outset, on the basis of what you have just told us, that none of those matters impact on our submission. Turning to our submission, we represent the Queensland Local Government Superannuation Board, which is the trustee of the fund that looks after local government superannuation in Queensland, excluding the Brisbane City Council.

There is about \$1.8 billion in the fund and about 50,000 members all told. There are active and inactive members in that 50,000.

I would like to state the general principles of our board's approach to portability and to the associated choice of fund policy, because we do see the two as being linked. So the board agrees that portability is a desirable and necessary complement to choice of fund. It also believes that one measure without the other is undesirable and that it would be inefficient and counterproductive. The board also believes that there are some superannuation arrangements where the essential integrity of members entitlements is reliant on the fund maintaining some certainty of membership and that there is a serious risk of those members entitlements being adversely affected if this certainty is removed.

Unfunded public sector funds and defined benefit funds, for example, have already been recognised as falling within this category and have been specifically excluded from both portability and choice of fund. The board would argue that active accumulation benefit members in our scheme would also come within such an arrangement, and the board welcomes the opportunity to explain why it sees that it should be excluded from the proposed portability regulations.

As I said, the scheme has about 50,000 members, who are divided into three main categories: defined benefits, which has about 9,000 members; accumulation benefit members, 21,000; and retained benefit members, 23,000. Two of these categories are unaffected by the proposed portability arrangements, and they are the defined benefits members and, of course, the retained benefit members. The defined benefit members have been excluded and the retained benefit members already have portability as such because they can move their money at any time. They have left the organisation, the employer, left their money in the fund and can move it around. I make the point that our fund maintains about 70 per cent of the moneys in the fund, on people leaving.

The local government superannuation scheme is governed by state legislation under the Local Government Act, which has two constraining and contrasting influences on the operation of the scheme. One is a limitation on membership, which restricts membership to local government employees other than employees of the Brisbane City Council. The membership is also compulsory. Section 1183 compels all permanent employees to contribute six per cent of their salary to the scheme. So only a restricted category of people are able to join our fund, but those who work within local government, apart from BCC, must join.

In 1998, the office of the Assistant Treasurer concluded in written advice to the board that the special circumstances of our fund warranted a specific exclusion from the operation of the proposed choice of fund legislation. In the same year the Australian Taxation Office also acknowledged this issue of exclusion from the proposed choice of fund legislation. I would like to read a letter from the office of the Assistant Treasurer, dated 30 April 1998. It states:

The choice of fund legislation is contained in Schedule 5 to the Taxation Laws Amendment Bill ... A number of amendments were made to the Bill during its second reading debate in the House of Representatives on 2 and 8 April 1998. I can now also advise that the Assistant Treasurer has announced that the introduction of choice of fund measures will be delayed. ...

In relation to the issue you raised in your letter, I offer the following comments.

The Government has proposed an amendment to the legislation to provide that contributions made in accordance with prescribed laws are made in accordance with the proposed choice of fund requirements ... This amendment will overcome a potential problem facing some employers who are required to contribute to a particular superannuation fund on behalf of their employees, and who would be required to contribute to another fund under the proposed choice of fund legislation. In such cases, an employee will be relieved from the need to comply with the two regimes. ...

Under this proposed new subsection ... it seems that the law you refer to may be eligible to be prescribed under regulations.

So the local government superannuation fund, subject to being prescribed, would not have to comply with the choice of fund legislation. With portability and no choice—one without the other—it really does not work. I would like to pass to my colleague now to further enhance the submission.

**Mr Carpendale**—We should also mention, I guess, that, in 2002, a national competition policy review was undertaken of the Local Government Act and its monopolistic provisions. The conclusion of that particular investigation was that the provisions satisfied the public interest test and, in fact, that they operated in the best interests of scheme members. So, in conclusion, from both the choice of fund perspective and the national competition policy perspective, there have already been reviews which have found that the Local Government Act provisions satisfy those requirements.

We would like to now turn to how the individual members of LG Super are affected and how they might in fact be advanced or advantaged by the fact that there is certainty of their membership in the scheme as guaranteed by the Local Government Act. Firstly, the growth in the size of the scheme has created economies of scale that are passed on to members through administration fees, which, at 0.15 per cent, are amongst the lowest in the superannuation industry. In terms of investment, this same certainty of membership has allowed the board to invest with a long-term growth strategy that has added approximately one per cent per annum to the retirement savings of LG Super members over the last 10 years. That one per cent per annum represents the difference between the average return from a growth fund investment and an average conservative fund investment over the last 10 years to 30 June 2003, as in the published InTech survey.

To level out the extremes of the high growth investment strategy for participating members, the board has used a crediting rate smoothing policy. Under this arrangement, members who leave in the short term are protected from the high volatility associated with the growth oriented investment strategy. More than 97 per cent of active members in the category we are talking about—the accumulation benefit group—have selected the growth-smoothed investment strategy, which is the board's default option for that particular group. The continuation of this arrangement is heavily reliant on the ongoing commitment of funds. The board is able to adopt such a long-term approach only because members' funds are guaranteed to remain with the scheme until they terminate local government employment.

Unless the active accumulation benefit category of the scheme membership is excluded from the proposed portability regulations in the same way that Peter mentioned would happen under

choice of fund, the adverse consequences for the scheme members would be as follows. Firstly, there will be an inefficient and disruptive disconnect between what members can do with their accrued benefits, that is, what would be allowed under the portability regulations, and what they can do with their ongoing contributions, that is, what is excluded under the proposed choice of fund regime. Secondly, the economies of scale achieved by LG Super to the advantage of scheme members would be eroded by the one-way impact of portability on our scheme. Existing moneys may be transferred out of the scheme, but state legislation restrictions would prevent replacement funds from flowing back in via new membership groups.

Thirdly, the at-call nature of members' accrued entitlements will force the board to abandon its growth oriented investment strategy combined with crediting-rate smoothing as a default option for active accumulation benefit members resulting in an earnings loss of up to one per cent per annum. The board does support the dual implementation of choice of fund and portability in arrangements where unfettered choice can operate effectively. Unfettered two-way choice will never apply to LG Super because state legislation restricts who can join the scheme and also compels the future contributions of local government employees to continue to be directed to the scheme. In summary, the board believes that it is in the best interests of the superannuation entitlements of local government employees in Queensland that the portability regulation exclusion granted to active defined benefit members be extended to also cover the active accumulation benefit membership category of the scheme, and we seek your approval for this measure.

**CHAIR**—Thinking through the logic of it, basically those arguments would apply to any super fund, though, would they not?

**Mr Smith**—Some of the arguments may, but there is a unique aspect in that local government—

**CHAIR**—I am not arguing against it; I am just saying that you are showing us a pathway for treating active membership.

**Mr Smith**—Our submission has choice of fund and portability combined. With our fund being exempted from choice of fund because of state legislation, portability by itself just does not sit well at all.

**Mr Carpendale**—The other issue is that we are different from most other funds in that other funds do not have their scope of influence restricted by state legislation. If portability were to apply to them, yes, they may lose some moneys, but they can also gain some moneys by seeking new categories of membership. That avenue is cut off to funds like ours, where state legislation says, 'These are the parameters of your influence. That's as far as you will go; that's all we want you to do. We don't want you to do anything more. You're for that particular category of people.' So, some of that money goes away. Portability is a one-way issue in relation to our fund.

**CHAIR**—You state that approximately 70 per cent of inactive peoples' moneys remain in your fund. Do you feel that you have a moral obligation to notify people where there is a request to transfer money to another fund which in your view is certainly not performing as well as your fund?

**Mr Smith**—You can make comparisons one year to the next. We might be better than the transferee fund one year but not the next. We emphasise the low-cost fee nature of our fund and we tell people of the past earnings, and the majority of members do stay with us for the long term.

**Senator BUCKLAND**—Is that 0.15 per cent the total fees?

**Mr Smith**—That is the administration fee. The investment management fee would be about another 0.5 per cent on top of that. It all depends on the strategy, but I am just talking about the high-growth strategy being a total charge of 0.65 per cent, which is extremely low.

**Senator BUCKLAND**—Extremely low? Educate me if you would. What are some of the others that you are aware of?

**Mr Smith**—I will go to the other extreme and say that a retail fund could be two per cent or more.

**Mr Carpendale**—There was recently a working paper done by APRA in relation to superannuation fund returns over the 10 years ending 30 June 2002. The 0.65 per cent that our members are paying was certainly right at the low end of that category. I think the average combined fee was 1.2 or 1.4 per cent. The retail funds were closer to 1.8 per cent.

**Senator BUCKLAND**—Do you think that the membership of your fund is aware of this low fee and the impact of that on their overall superannuation?

**Mr Smith**—I believe the more informed member is, but I think it behoves us to tell the members more about that today, particularly in today's investment environment, because that is a given; that is a certain amount. If you make the comparison with a retail product, let's say, you have a one per cent jump on the pack. They have to make up one per cent before they can get close to us. We still believe that our investment strategy over the longer term will outperform others. Again, we are hoping that economies of scale come into that as well, but we believe our past returns also support staying with our fund. In regard to the 70 per cent we mentioned earlier, there is not exactly a benchmark against which we can judge whether that is a good figure. Intuitively, I believe retaining 70 per cent of people who could leave the fund money in our retained benefit products seems to be a pretty good strike rate.

**CHAIR**—What was your return for the last 12 months? Are you in positive territory?

**Mr Smith**—The overall fund was negative 1.81 per cent. That is for the composite of all the strategies. That figure does not relate to any one of the strategies. I am saying collectively that is what we earned. We have a cash strategy and it would have got to 3.6 and so on.

**CHAIR**—That would be in positive territory?

**Mr Smith**—The 1.8 per cent was negative and the cash of course was positive.

**CHAIR**—Was your balance positive?

**Mr Smith**—I recall that it was 0.73 per cent.

**CHAIR**—Was your growth slightly negative?

**Mr Smith**—Yes.

**Mr Carpendale**—The growth was 1.7 negative, but the growth smooth strategy—the category that applies to most of the people in the category we were talking about—uses reserves and we are crediting 2.04 per cent positive for those members.

**CHAIR**—That is good. So, for the bulk of your members you are producing positive results.

**Mr Smith**—That is correct. That was the point that John was making in his part of the presentation.

**CHAIR**—I just wanted to emphasise that.

**Mr Smith**—If people can move out, we would have to forego smoothing and it would be very difficult because people would be selecting against us going in and out and so on.

**CHAIR**—That is a credit to you. I think the better funds have certainly come back into their cash. They are balanced and into positive territory—not by huge amounts, but it is a good sign for superannuation when so much negative press is being written about superannuation. At the moment, people are losing a little confidence. I think the funds and this committee have a responsibility to point out the good news when it is around.

**Mr Smith**—This year we have used reserves to get there, to get on our smoothing.

**CHAIR**—You have sacrificed crediting rates in the past to achieve that.

**Mr Carpendale**—Correct.

**CHAIR**—It is all done to keep confidence by your membership in the fund.

**Senator BUCKLAND**—From your submission, I understand what you are saying about exemption if these policies were introduced. I understand the state based nature of it and take that into account as well. Do the industrial relations implications have any bearing on this?

**Mr Carpendale**—I believe that particular issue was addressed in the public interest test that was conducted under the national competition policy review, which looked at provisions of the local government act that provided the monopoly that local government employees in Queensland, aside from Brisbane City, had to belong to our scheme. That was certainly looked at.

**Senator BUCKLAND**—Was that contested at all by anyone?

**Mr Carpendale**—In terms of the public interest tests that were conducted, there were a range of stakeholders across a range of different involvements with the scheme who were consulted and given the opportunity to provide submissions. Certainly two of the major unions that represent employees of the scheme made submissions. The employer group—the Local Government Association of Queensland—made submissions. All of those submissions supported the status quo. There were two other options that were suggested as alternatives to the status quo, and the overall summation was that the status quo better met the public interest test than did the alternatives that were looked at. Those alternatives included allowing local governments to use another scheme rather than our scheme, and a third option was to allow our scheme to operate outside the scope of local government employment—that is, allow them to take in extra membership outside that group. Again, that was rejected and the status quo was maintained.

**Senator BUCKLAND**—You were talking about the approximately 50,000 members that you have and you made references to the ‘non-active’ members. Why are they non-active? Is there a purpose? Is it just that they have left and not picked up their cash or rolled it over somewhere else?

**Mr Smith**—No. It has been a deliberate action of theirs to say that they want to stay with LG Super as their superannuation provider. Quite a few of those members have taken the allocated pension route through our fund. Our superannuation scheme introduced an allocated pension back in 1993. I think it was the first or the second super fund to do so. I guess people have trust in the fund and have shown that by staying with us.

**Senator BUCKLAND**—It would be indicative of the confidence they have in the fund, wouldn't it?

**Mr Carpendale**—Certainly. In the industry, the term ‘active’ generally means the people who are in employment and ‘inactive’ just means those who are still in the scheme but who are not actively contributing because they have ceased that employment.

**Senator BUCKLAND**—Have you had any approaches from fund members saying that they would like portability or they would like to go elsewhere? Have there been approaches from individuals or groups?

**Mr Smith**—I cannot say that there has not been one, but they would be counted on one hand. Would that be reasonable to say?

**Mr Carpendale**—I have not personally seen one, but I am sure that there has been one.

**Mr Smith**—There is no groundswell there at all.

**Senator BUCKLAND**—We are talking now about 0.65 per cent for your fees; if portability were to come in, do you believe that the fee structure would have to increase to cater for the movement of funds in and out?

**Mr Smith**—I believe it would and I believe that we would have to not just have a level fee scale across the board but that, for those taking advantage of portability, we would have to charge them more as opposed to the people that just stay with us. There was, as Senator Watson

explained to us earlier, a proposed change to the regulations once a year, but I can still see that our fund, being exempted from the choice side of things but having to apply portability, would be having moneys still coming to us but once a year having to transfer them out for that person who has gone to another arrangement. Once a year, each and every year, in respect of that one person we would have a transfer.

**Senator BUCKLAND**—I am just thinking about the impact. It needs a little bit of thinking through and I do not know that I am going to be able to do it here. If that were the case—that you had portability, where members could transfer out—surely it would lead you to believe that non-local-government people would have the ability to transfer in.

**CHAIR**—Only if they had the status of what is known as a public offer fund, so they would have had to have changed their constitution.

**Senator BUCKLAND**—That goes back to the earlier question I asked about industrial relations. That is quite a complex issue to get through.

**Mr Smith**—It comes back of course to the state legislation that restricts membership to local government. We believe that if we were just a public offer fund we would just be like any other fund out there, but we can offer something specific to local government people—as John said earlier, smoothing and those economies of scale. It is a fund set up for local government and it can offer some unique characteristics.

**Senator BUCKLAND**—I suppose I was just thinking on the run. Sadly, I do that sometimes. Again looking at that 0.65 per cent, I struggle with the idea that you could maintain the funds—and the fund, despite everything that has been happening, has not performed too badly. I struggle to see how you could get away with only applying the additional fee to exit and entry, because you need to maintain that base level of investment.

**Mr Smith**—Sure. I guess I am thinking on the run along with you on that issue. What I was meaning to say was that the people that want to have the portability should be bearing that additional cost in some shape or form and that as much as possible the people that stay with the fund long term should not bear a disproportionate share of that cost.

**Senator BUCKLAND**—But it has the potential to penalise that group of people.

**Mr Smith**—Yes, it does have the potential of increasing the base.

**Senator BUCKLAND**—It is sometimes dangerous to think on the run but I think there are dangers in that process.

**Senator LIGHTFOOT**—I wish to ask Mr Smith or Mr Carpendale a couple of simple questions with respect to the two local authorities having separate entities as far as superannuation is concerned. With the superannuants with transportable superannuation being able to cross from one to another, do you expect to take some from Brisbane City Council? Would you lose some? Why isn't there just one, given the economy of scale?

**Mr Smith**—It really goes back in history. The Local Government Superannuation Scheme—our scheme—is set up under a different act of parliament, and it is really historical. The Brisbane City Council fund has about 8,000 members and about \$650 million. There have been discussions as to joining those funds together—the natural alliance with the natural partner—but that is not our decision of course. Other state organisations have had city council funds—whatever state it might be—come into the statewide fund, but that does not happen in Queensland at this stage.

**Senator LIGHTFOOT**—So you would have probably, just from an interest point of view, ascertained how well their fund was doing. Can you tell the committee how that compares with yours on a per capita basis, if that is possible?

**Mr Smith**—\$650 million is the fund—

**Senator LIGHTFOOT**—as opposed to \$1.8 billion.

**Mr Smith**—Yes. There are various strategies that we have in terms of choice of investment strategy. Without going into all of them, we were about line ball with their rate of return last year. Their cost benefit arrangements would be about the same as ours, and bring the two together and you have further economies of scale. So that is one area where—and again I am not putting this forward at this moment—that is a natural partner that we have. But we would not be planning to go to public offer with our fund.

**Senator LIGHTFOOT**—That is \$2½ billion combined, roughly, and growing. I imagine it is growing.

**Mr Smith**—Yes.

**Senator LIGHTFOOT**—It would want to be growing. The superannuants would hope it was growing. Do you talk regularly between the two authorities?

**Mr Smith**—Yes, we do. I will go so far as to say that there is a meeting tomorrow. That is as much as I can say.

**Senator LIGHTFOOT**—Insofar as you have had a chance to look at the new legislation with respect to portability, do you think that is going to facilitate one body?

**Mr Smith**—It would not be facilitated by the portability legislation; it would be an amalgamation of funds to make one local government fund.

**Senator LIGHTFOOT**—So the recent legislation would not have any bearing on it?

**Mr Smith**—No, it would just come under the one trustee umbrella. But I do emphasise that that is under discussion at this stage.

**Senator LIGHTFOOT**—You probably are one of the bigger, if not the biggest, schemes in Queensland now. Would this make any difference?

**Mr Smith**—I think there is a little bit of a league table. Whereas we are around 28th, we would be about 20th—something of that order. BCC, with their 650, would be about 50th or 56th.

**Senator LIGHTFOOT**—That is very interesting, thank you.

**CHAIR**—There is no doubt that there are quite a lot of economies of scale in amalgamation, and I think over the years we will see more and more. The fact that government has capped some of their APRA fees works very much to the detriment of the small- to medium-scale funds. Those sorts of factors alone give administrative advantages on terms of scale. On the other hand, boutique funds that have flexibility can do very well. But those that are in the middle really are fighting this cost battle all the time.

**Senator CHERRY**—You probably answered this question earlier—and I apologise for being a bit late—but you say in your submission that you are classified as a funded public sector defined benefits scheme. Is your scheme completely exempted under the regulation as promulgated yesterday? Do you want to take that question on notice if you cannot answer it now?

**Mr Smith**—These were the changes that you indicated?

**Senator CHERRY**—Yes.

**Mr Smith**—Those changes do not impact on the submission that we put up.

**Senator CHERRY**—There is a complicated definition about defined benefit, so I just was not sure.

**Mr Smith**—We have not seen that. We understand that portion of the Local Government Superannuation Scheme, the defined benefits section, was always going to be excluded. We have not seen the detail of the proposed amendments. If the amendments changed that definition such that our entire scheme was excluded then there would be no need for our submission, to some extent. But the summation that we saw of the changes overnight did not make reference to a change to the definition of ‘defined benefit scheme’, so we cannot really comment on that.

**Senator CHERRY**—Presumably, if it does, you will let us know.

**Mr Smith**—Certainly, and the Chair did invite us to make a supplementary submission if, in fact, there was such a change.

**CHAIR**—Thank you very much for coming down. We very much appreciate your submission, and I think you have helped the committee quite a lot.

**Mr Smith**—Thank you very much.

[2.39 p.m.]

**ABRAHAMS, Mr Derek Laurence, Consultant, Professional Financial Solutions**

**FITZPATRICK, Mr Martin Peter, Consultant, Professional Financial Solutions**

**HOLLAND, Mr John, Compliance Officer, Australian Administration Services**

**KORCHINSKI, Mr Stuart, Chief Executive Officer, Australian Administration Services**

**CHAIR**—Welcome. This morning the committee became aware of some additional regulations put out by Treasury. Have you seen them and had time to assess them with regard to the impact on your fund?

**Mr Korchinski**—We have not seen them.

**CHAIR**—If you have not seen them, perhaps I should read this statement to you to help provide a bit more information. It states:

The Government's revised Portability Regulations were gazetted this morning—

that was yesterday morning—

together with accompanying Explanatory Statements. I wish to note that the final regulations include a number of revisions to the draft regulations from which we have been working. In particular, the SIS Amended Regulations 2003 include three major revisions:

1) Revised disclosure requirements: Regulation 6.34(2), introduces new requirements relating to disclosure of fees and charges by trustees, and the impact of a transfer on a benefit statement.

2) Partial transfers out of the account: Regulation 6.35(1)(b) provides that a trustee of a fund may refuse a request for a transfer where the fund will hold less than \$5,000 following the transfer.

3) Transfers out of an active account—Regulation 6.35(1)(c) provides that a trustee of a fund may refuse a request for a transfer where a transfer has already occurred in the last 12 months.

We would invite you and all the other participants to make a supplementary submission on these issues, if you wish, because they obviously could impact on your recommendations or your approach to portability. I now invite you to make an opening statement.

**Mr Korchinski**—Thank you very much for the invitation to appear before the committee. This is the first occasion on which I have appeared before the committee in my role as the chief executive officer of AAS. AAS became part of KAZ Group Ltd in 2001 following its acquisition from AMP. Prior to that, it was part of the AMP group. AAS is a superannuation administrator specialising in industry funds. Through 700 employees based in six states, we provide superannuation administration and customer services to 3.4 million members and 165,000

employers. This background information helps, I hope, to explain the important role that AAS plays in the superannuation system.

As superannuation continues to evolve and become more complex, efficient administration will become even more important for members and employers. Originally, most superannuation administration was undertaken by large financial institutions, such as life offices, as an ancillary activity to their core fund management and insurance activities. Today, superannuation administration needs to operate profitably without financial support from other business activities.

When AAS was part of the AMP group, public positions usually reflected the view of the entire group, rather than just the AAS segment, hence AAS's views were not widely known. In recent times, AAS clients have encouraged more direct participation in key issues, such as portability, that have a strong link with administration. We see our role in the superannuation debate as providing expert commentary on relevant issues on behalf of a clients.

Turning to our submission, I wish to stress several of the key points it contains. Firstly, we see portability and choice of fund as being inextricably linked, from several viewpoints, including administrative feasibility and member understanding. While it would be possible in theory to introduce portability without choice of fund, we would expect that approach would lead to increased costs for members with little in the way of improvement and benefits. Secondly, if portability is introduced without choice of fund there would be an increase in the instance of multiple accounts for members, not a reduction. Portability already exists for most fund members; the main change from the draft regulations would be to allow members to move existing superannuation benefits between funds while remaining with their current employer.

Thirdly, we have concerns that members may be severely disadvantaged, because retail superannuation providers with large marketing budgets would be the greatest beneficiaries of a portability regime and the members of non-profit funds would potentially be the largest losers. Many financial planners are reluctant to recommend non-profit superannuation funds, such as industry funds, which do not pay commissions. These concerns are supported by a recent report prepared by ASIC and the Australian Consumers Association in February 2003. This report on financial planning stated:

... clients' interests did not appear to be the sole factor in the plan strategy or product selection. They characterised this practice as '*commission-driven product selling, not impartial advice*'.

The report also stated:

Many plans did not recommend the lowest cost option available. As low cost options pay no commission, this raised some suspicions about the influence of commission on advice. For example, no adviser recommended switching to a nonprofit, industry superannuation fund.

My final point addresses the impact the new regulations would have on the costs of member benefit protection, which is a compulsory cross-subsidy for members with low account balances. These costs are relatively high for industry superannuation funds which contain high proportions of younger members, casuals and others with low balances. As previously written, the regulations did not address the issue adequately. In particular, I propose member benefit

protections be reviewed in conjunction with the introduction of portability and choice of fund—and the minimum balances that were mentioned earlier in the regulations were along the lines of our thinking. Thank you again for the opportunity to take part in the consultation process. I would be pleased to respond to any questions you might like to ask about our submission.

**CHAIR**—Thank you for your presentation. It is always good to hear from administrators. On this occasion we have heard from two administrators—you and Watson Wyatt. One issue that I do not think you referred to in your presentation—I think you addressed it in your submission—was the impact of the surcharge. Could you just indicate the impact of portability from an administrative point of view. It might be outstanding, but there is a surcharge obligation if through portability someone transfers the account to another fund. Is that a problem?

**Mr Fitzpatrick**—Where it is done on a partial basis, the requirement to split and keep track of it from that point of view then becomes an issue. John, do you want to further expand on that?

**Mr Holland**—I think the answer to your question is in the regulations that came out yesterday. If a trustee is permitted to refuse a request for portability, a request for transfer, if it is under \$5,000 the surcharge issue will disappear—you will not have that issue. Rather than me going into the technical detail that would exist if that provision were in the regulations, I will just say that if trustees will accept the opportunity or the possibility to refuse a transfer if no balance of \$5,000 is left behind, that issue will not exist. So we are happy with the change that you mentioned 10 minutes ago, because it will resolve the surcharge problem.

**CHAIR**—Do you think that will solve the surcharge problem?

**Mr Fitzpatrick**—It would help dissipate it, but I think there would still be some issues. The pushing of money around the system that we already see—where the liability for surcharge on contributions is progressively passed on to different administrators—I think potentially will be exacerbated, because there will be more pushing of contributions around as there are partial payments pushed through the system.

**CHAIR**—That was my concern.

**Mr Fitzpatrick**—I think that is a valid concern.

**CHAIR**—How will you handle it? Just by writing to the tax office and the fund who you believe to be the recipient of the moneys which you previously held?

**Mr Korchinski**—I think we would have to discuss that as an industry to come up with a common rule that would apply in that situation. It would involve trying to enforce a uniform approach right across many administrators. Our concern is obviously the administrative costs associated with implementing a unified and uniform approach.

**Mr Fitzpatrick**—It will be more cumbersome. It will add to costs. You will try to deal with it as efficiently as you can, but it will add to costs.

**CHAIR**—Is it worth the committee inquiring of the tax office how they intend to handle it?

**Mr Korchinski**—It would be our recommendation that you do speak to the ATO about that. We are aware that the ATO has been spending more and more time on the whole issue of receiving of surcharge, and it has been in the context of trying to automate more of that in terms of the receipts from various funds, so we would see the ATO as being a good driver of uniformity in that particular area.

**CHAIR**—Where you are in receipt of a notice of assessment, would you be obliged to notify the member that he cannot transfer all his money out, because there is an obligation there for you to meet?

**Mr Korchinski**—Potentially the trustee could make that election. Alternatively there would have to be rules that would apportion the payment or the balance between the various funds. That is the complexity that we would find costly and cumbersome.

**Mr Fitzpatrick**—The member would be at the end of the chain, as he is now, if the surcharge liability were passed on and on and did not find a home. Ultimately, if there is a benefit paid, then it comes back to the tax office to deal with the individual concerned.

**Senator CHERRY**—In your submission you talked about the impact of portability on insurance and how it would change that. I would be interested in hearing you expand on that. You have probably gone into it in more detail in your submission than any other witnesses have. Could you go through what impact that will have on insurance cover and premiums from your point of view.

**Mr Korchinski**—There are a couple of points. I will start with the first one. We are concerned about the situation where a member decides to move a portion or all of their asset to another fund but forgets about the fact that there is insurance, or was never even aware of the fact that there was insurance in their current fund. If they move to a fund with different insurance cover, they potentially could be disadvantaged. There is an educational requirement for a person to go through and to understand what the potential impact is of the transfer. However, a more significant issue is where, through ignorance, they transfer an amount or the majority of an amount and it does not leave enough in their previous fund to pay for insurance cover. If they move to a fund without cover, thinking that they did have cover in the new fund, and all of a sudden find that they did not have cover in the previous fund either, then we have a consumer, a member, without insurance protection whatsoever. We receive a lot of queries and questions from superannuation members about insurance. It is not a commonly well-understood area, much like superannuation.

**Senator CHERRY**—One often wishes the industry funds never got into the area in the first place. It would certainly make administrators' jobs much easier.

**Mr Korchinski**—I suppose so, but when you look at the entire insurance process, it is a pretty practical one for large groups.

**Senator CHERRY**—The other question was to do with your first section, where you talk about the background of the current situation with portability and you suggest that the 90-day benchmark, the minimum standard in this regulation, is way below what industry standards are. I asked one of the earlier witnesses these same sorts of questions: how many transfers would be

done quickly within 30 days; how many would be prolonged and why; essentially what is wrong with current portability; and what difference would this regulation make outside of the area of active accounts?

**Mr Korchinski**—I guess our comment was about the fact that 90 days to action a request from a member would be generally considered to be poor service. To the extent that any superannuation fund adopted a minimalist service approach, I think it would be reasonable for superannuation consumers to think that we had not put in place a reasonable service standard. We would see some downsides to superannuation as a product in general because of that.

**Senator CHERRY**—Do you think there would be slippage out from the current industry benchmarks towards that 90-day benchmark? There is always the worry when you regulate something that it might slip in the other direction.

**Mr Korchinski**—Service standards are directly related to cost, and if there is an industry or countrywide expectation that you get paid within 90 days then I suppose there would be some that would look to say that that is a reasonable standard—

**Senator CHERRY**—89½!

**Mr Korchinski**—and say, ‘It is legislated and you can’t blame me, so don’t complain, Mr Consumer.’ I would have to say that the majority of people would say, where they have current standards that fall within five days, that it is probably harder to change the system to allow for 90 days.

**Senator CHERRY**—There has been some discussions in some submissions about the need for a transfer protocol in addition to a portability standard. Do you have any views on that?

**Mr Korchinski**—The whole transfer protocol has been a matter that the industry has looked at for many years. It is conceptually attractive but very difficult to implement. The problem with the implementation is primarily due to the fact that a lot of the transfer processes are computerised—whilst we do have a standard protocol in place, for many of the funds the costs to actually move to that protocol are excessive, and there is no attraction in the short term to offset that cost. It is one of the disappointments within the industry, because in the majority of cases we issue cheques to transfer when there should conceptually be a clearing house approach, much like the way cheque clearing occurs.

**Senator CHERRY**—One of the things which I have been fascinated with in the submissions to this inquiry is what is broken in terms of the current portability arrangements outside of the area of active accounts. I remember being briefed about transfer protocols seven or eight years ago—as would Senator Watson—by lots of very enthused and excited industry lobbyists, and nothing has happened since. Do you think that would be a more useful area of reform than some of the things dealt with in this regulation?

**Mr Korchinski**—Transfer protocols becoming automated in the industry would reduce costs within the industry and therefore, unlike portability, would be beneficial to consumers.

**Senator BUCKLAND**—You talked about portability and the choice of fund being linked, and that is an integral part of it as you see it: you cannot do one without the other. This morning we heard evidence to suggest quite the opposite to that. Can you tell us why you think you are right in that assumption, taking out my bias, whichever way I might lean?

**Mr Korchinski**—When we looked at the proposed benefits of portability and how portability would work in practice, we identified several benefits that we did not think would actually arise. The first one was the desire to reduce the number of accounts out there at the moment. Again, portability seemed to us to result in a member potentially keeping one account with their existing fund and setting up another account with another fund—so, all of a sudden, one member has two accounts, yet the choice of fund proposal effectively says that you would move from one account to another account and still only have one account. We thought that separating the two would actually end up creating additional accounts that were not required and, in fact, were contrary to the intention of both proposals. Effectively, we saw portability as *de facto* choice in any event. With portability you have the problem that fees would be charged to the members who exited the fund or transferred a certain percentage of their funds. That was ultimately going to be more expensive than choice of fund.

**Senator BUCKLAND**—Do you have any idea of what the increased fees would be, particularly if it were introduced as a singular piece of legislation or a regulation?

**Mr Korchinski**—Without the benefit of seeing the legislation or regulations I would have to say that on balance it would be similar to the transfer fees or the benefit payment fees that currently apply within the industry. There would be a one-off cost to accommodate portability given the nuances of the regulations. Again, we are not able to assess what those costs would be, but we suspect that they would be considerable.

**Senator BUCKLAND**—Considerable? Are you talking about 0.1 per cent or 0.05 per cent? I know that is very difficult to answer.

**Mr Korchinski**—The benefit payment costs that the industry superannuation funds charge their members range from zero to \$50 to \$75 per transfer. The concern we had in aggregate was that, if someone were keen to be out of their existing fund and they set up an account with a new fund and every three months emptied their current fund and transferred the money into the other fund, there are going to be ongoing benefit payment costs to the consumer. Depending on the level they were set at they might prohibit the actual transfer. It may get uneconomical. Alternatively they would just eat into the ultimate retirement income that would be available to that particular member.

**Senator BUCKLAND**—If you had a fund hopper paying that sort of money, particularly when it is around \$75, looking around for a higher return could almost negate the member's benefit, couldn't it?

**Mr Korchinski**—Yes, that is quite right.

**Senator BUCKLAND**—This is a bit embarrassing. I think I have run out of questions!

**Mr Korchinski**—I have one other point just to finish that off. It relates to member benefit protection costs that our funds incur. Several of them have requested me to raise this issue here. In a sense, the \$5,000 limit that the regulations now suggest obviates our concern. Our original concern was that you would have people leaving less than \$1,000 within their fund, and the cost of member benefit protection for the fund would then increase as the number of those members increased within that fund.

**Senator BUCKLAND**—You are probably in a better position to answer this question than most who are appearing before us at the moment: have you had any applications or inquiries from your members regarding being able to swap between funds?

**Mr Korchinski**—Yes.

**Senator BUCKLAND**—What do the inquiries involve—mainly to see whether they can get a better deal?

**Mr Korchinski**—Primarily. There is not a lot of it, because generally speaking it is not a top-line topic. But when the account statements get sent out once or twice a year, depending on the fund, you will get those queries coming through to the call centre by people wanting to understand the situation.

**Senator BUCKLAND**—Do you think the people making the inquiries are aware of the fees and structures? You mention that the beneficiaries of this would be the financial planning sector. Do you think that the people making the inquiries are aware of the fees that they would attract?

**Mr Korchinski**—Yes, increasingly so. Our understanding or belief is that that has primarily increased over the last several years due to two things. One is an increase in publicity—in newspapers and on radio—about superannuation and returns being less than they have been historically. And there is that latter point itself, so when the statement does come out and they see they have a \$10,000 balance and they have made \$500 in investment return, offset by an administration fee of \$50, or offset by an administration fee of \$1,000, you get two different reactions. Clearly, the one where the administration fee exceeds the investment income elicits a much more vociferous response.

**Senator BUCKLAND**—Colourful conversations on the phone, no doubt.

**Mr Korchinski**—We tape those calls now, with permission.

**Senator BUCKLAND**—In general, do you think fund members, particularly those who are susceptible to the lure of glossy advertisements on TV about financial planners, with catchy phrases which try to attract you to a fund, are aware to some of those difficulties?

**Mr Korchinski**—I would like to say yes, but I am afraid that I do not think they are as aware of the costs associated with non-industry funds.

**Senator BUCKLAND**—I might leave it there, Chair, or I might get into deep water here.

**CHAIR**—Thank you very much for appearing before the committee.

**Mr Korchinski**—It was a pleasure.

**CHAIR**—We will have a break for afternoon tea, and we invite you to join us.

**Proceedings suspended from 3.08 p.m. to 3.29 p.m.**

**HRISTODOULIDIS, Mr Con, National Manager, Policy and Government Relations, Financial Planning Association of Australia Ltd**

**CHAIR**—I welcome representatives of the Financial Planning Association. I take this opportunity of thanking your association, especially your CEO, for organising a very informative meeting of three very qualified financial planners from the suburbs of Sydney, rural New South Wales and Western Australia. Each had a very different practice but highlighted the competent approach financial planners take towards their clients and the way they go about their business. It was very informative and helpful.

**Mr Hristodoulidis**—Thank you. I will pass that on to Mr Breakspear.

**CHAIR**—I commend you on the initiatives you have taken in raising the bar and the standards. I think it is good for the industry and good for the association, so thank you very much. Mr Hristodoulidis, are you aware that yesterday some additional regulations were gazetted by Treasury?

**Mr Hristodoulidis**—No, I am not aware of any gazetting of regulations from yesterday.

**CHAIR**—That being so, I will acquaint you with a summary of those portability regulations. They state:

... the final regulations include a number of revisions to the draft regulations from which we have been working. In particular, the SIS Amendment Regulations 2003 include three major revisions:

1) Revised disclosure requirements: Regulation 6.34(2) introduces new requirements relating to disclosure of fees and charges by trustees, and the impact of a transfer on a benefit entitlement.

2) Partial transfer out of an account: Regulation 6.35(1)(b) provides that a trustee of a fund may refuse a request for a transfer where the fund will hold less than \$5,000 following the transfer.

3) Transfer out of an active account: Regulation 6.35(1)(c) provides that a trustee of a fund may refuse a request for a transfer where a transfer has already occurred in the last 12 months.

That is a very shorthand summary of those changes. We must of course refer you to the full extent of the regulations but, as a courtesy to you, we should point out that there have been a number of substantial changes introduced by Treasury at this stage and, unfortunately, they did not advise the committee.

**Mr Hristodoulidis**—I thank you for the update on those regulations. On the initial reading of them, I think they are good changes to the regulations. We did make a submission to Treasury on the draft regulations. On points two and three we made reference to having some sort of minimum standard if people do not make a full withdrawal when they are using the portability transfer. We also made some comments about the number of transfers per year to keep down the administrative costs. On my initial reading, my initial reaction is that they are welcome changes to the regulations.

**CHAIR**—We invite you now to talk to your submission.

**Mr Hristodoulidis**—I would like to make two apologies. Obviously, one is for Mr Ken Robinson, who unfortunately could not make it at the last minute and is still in Melbourne today. I also would like to apologise for the very late lodgement of our submission. I think I sent it through last night to Stephen who was on his plane to Sydney. I apologise for that and any inconvenience that may have caused the committee.

I would like to make a few opening comments and make some points in regard to two parts of the terms of reference. Let me start by saying that the Financial Planning Association is the peak body representing some 14,500 financial planners across Australia. We have always supported and continue to support greater flexibility in investment in superannuation choices for all Australians. As part of this support, we welcome the draft regulations and the amendments that have just been read to those regulations in terms of implementing greater superannuation portability in Australia.

We also support the linking of the introduction of the superannuation fund choice legislation with the superannuation portability regulations. We believe that these two measures are complementary and must be introduced together, and that the start date of July 2004 is achievable. This is based on the notion that, under the new superannuation fund choice regime outlined by the Minister for Revenue and Assistant Treasurer in May 2003, there is a much more passive form of choice than previously outlined in the draft bills.

The FPA commissioned Roy Morgan Research in November 2002 to conduct a survey of Australian attitudes to superannuation. In the findings of the survey, there was significant support for both superannuation fund choice and portability. Respectively, 71 per cent and 88 per cent of respondents supported super fund choice and portability.

As I said earlier, I would like to spend a few moments speaking to two elements of the terms of reference. The first I would like to address relates to item No. 3, 'The desirability and practicality of the portability regime in the context of the existing structure of the financial planning industry.' The FPA, as you are all aware, were disappointed in some of the findings of the ASIC/ACA shadow shopping survey findings in February this year; however, we believe much water has passed under the bridge since then. We believe the FPA has been the single most important institution responsible for raising the standards of advice and practice in the financial planning industry since its inception 10 to 15 years ago.

As part of this ongoing commitment, we have recently introduced our professional partner program. The program has two main focuses, being the raising of standards and the lifting of consumer confidence. Through five campaigns which we believe will be the building blocks to improving the quality of financial planning advice, we intend to meet these objectives. The first campaign, which is on disclosure, we believe will deliver clear, concise and effective disclosure of fees and commissions by developing standard industry documents using common terminology and formats.

Our second campaign, which is about professionalism, will drive professionalism by focusing on education, ongoing training and a review of the FPA code of ethics and rules of professional conduct. I will come back to that campaign in a few moments. The third campaign, which is on

advice, will focus on the individual practitioners and provide them with the necessary tools on how to communicate advice to consumers. The fourth campaign is on the FSR transition, and we hope to have all members in the AFSL system by March 2004. Finally, the fifth campaign is centred on consumers. We hope that this campaign will build a comprehensive consumer education program by highlighting to consumers the value of financial planning advice and will show consumers how to receive quality advice.

However, the success of the professional partner program relies on acceptance by all stakeholders. To this end, the program was developed in consultation with our members and other key stakeholders. We surveyed our members on the final program and found very strong support. Over 90 per cent of members either strongly or very strongly endorsed the program. Under the FPA's professional partner reform program, the FPA has today announced a major initiative in the drive for greater professionalism. We are committed to promoting the CFP designation as the mark of distinction of a professional financial planner and the highest membership designation bestowed on individuals who meet the high standards of education, examination, experience and ethics. The CFP is the highest internationally recognised designation for financial planners in Australia. There are already 5,000 CFPs practising in Australia, and it is expected that this number will continue to rise, with more than 800 students having enrolled in the CFP program each semester in the last 12 months.

The emergence of specialist degrees in financial planning at both the bachelor and the master levels was a powerful signal that financial planning has gained academic recognition as a distinct occupation grouping. The availability of financial planning degree majors has reached the point where, today, the FPA announced a degree entry as the entry point to the CFP program in 2007. Hence, the FPA is confident that, together with its members and the professional partner program, the industry will continue to raise standards and be well placed to service the retirement and other financial needs of all Australians.

The second element I would like to turn to is consumer protection. The FPA believes that the Financial Services Reform Act provides world's best consumer protection. We believe that there is no need for further regulation; rather, we believe that legislators should give the FSRA an opportunity to bite. Specifically, and to address the issue of churning under a portability and greater choice environment, section 947D of the FSRA makes it clear that the government will not tolerate churning. It sets a high hurdle for disclosure and justification for financial planners to show to their clients the net benefits of any switch in investment products. This is reinforced in the recently released ASIC policy statement No. 175, entitled 'Licensing: financial product advisers—conduct and disclosure'. I would like to quote paragraph 175.91, which states:

In the case of advice to replace one product with another product or to switch between investment options within a product, we consider—

'we' being ASIC—

that the advice will generally be inappropriate if the providing entity knew or ought reasonably to have known that the overall benefits likely to result from the new product or option would be lower than under the old product or option. This applies where either or both the new product or the old product is a financial product for the purposes of part 7.7. Of course, we would be unlikely to reach this view where there are overall cost savings to the client that are likely to override

the loss of benefits. The determination of whether there are overall cost savings for the client must take into account all the circumstances, including the costs of the replacement i.e. making the switch.

We believe that is a very high benchmark for planners to achieve before they can switch their clients in their investment strategies.

Finally, the FPA believe in and support a well-funded education program of super choice and portability prior to their introduction. To this end, the FPA remain committed to working with ASIC on such publications as *Don't Kiss Your Money Goodbye*. They provide consumers with invaluable tips when dealing with financial planners. At this stage, I welcome questions from committee members.

**CHAIR**—Thank you very much. They are very reassuring words coming from the Financial Planning Association. I think it was helpful for you to draw attention to the provisions of the FSR; they are indeed a big advance on what we have and are probably world leaders. It is going to take a while for the whole industry to bed down those changes. Thank you for your approach; it has been very helpful. I think it addresses some of the concerns that a number of witnesses have raised in relation to the issue of churning.

**Senator CHERRY**—Do you think the portability regulation, as it stands, raises the same issues about the need for independent advice as the choice of funds legislation would raise. Are we dealing essentially with the same sorts of issues?

**Mr Hristodoulidis**—As I said in my opening comments, I think the two measures—choice and portability—need to be introduced together because you cannot really have one without the other. If you introduced portability, that gives employees the opportunity to bring across old superannuation funds that they may have into a new scheme. However, when they change employers, it does not necessarily mean that they will have the choice of fund. As I said, in the Roy Morgan research we conducted, 88 per cent of respondents said they would like to keep their superannuation fund if they were to change employment. Portability is important and there is high support for it in the community but you also need choice in case there are people who say, ‘When I go to a new employer, I do not want to go into that particular industry or corporate fund; I would rather choose my own fund.’

**Senator CHERRY**—One of the arguments that is being put for this regulation is that it will help in consolidation of accounts. Other witnesses we have heard this morning have argued that consolidation is not really a legal issue; it is a cultural issue, and Australians are just too lazy to keep an eye on their superannuation. From your point of view, what do we need to do to encourage consolidation?

**Mr Hristodoulidis**—For our members who deal with clients that may have a number of different superannuation accounts, it is both a cultural and legal issue. There are barriers in certain circumstances, where you cannot bring across funds into—

**Senator CHERRY**—Defined benefits type funds?

**Mr Hristodoulidis**—And industry and corporate funds as well. There may be some restrictions on transferring across. There are some legal aspects to it, but there is a cultural aspect

as well. About two months ago we actually introduced a tool kit on financial literacy, aimed at schoolkids. It is aimed at a year 9, year 10 level. It is about teaching people what rights and obligations they have under a superannuation regime, so hopefully by the time they get to the workplace they will have worked through this tool kit booklet and will have a better appreciation of the system and their rights under the system.

**Senator BUCKLAND**—You were talking about the changes that are occurring in the association, and I have to say they are a positive move. Are the changes going so far as to change some attitudes within the association's membership towards industry funds?

**Mr Hristodoulidis**—We have had this discussion with our members in the association, and there is no bias or prejudice against industry funds by our members. Basically our members are required to undertake due diligence on any product that they recommend. It is often the case with industry funds that they do not open themselves up to assessment by either the planners and their research houses or by other independent research houses. The first step to being recommended by a financial planner is that the planner can undertake an appropriate due diligence to ensure that the product meets any obligations they need to meet in terms of the clients' needs. We have had discussions with a number of industry funds about that and they have accepted that they need to open their books up and allow these due diligences to be conducted. At the briefings today, some of our members spoke—not directly to the senators, but to us privately—about some of their clients. One of our members gave an example of a client who had been offered to go into a HESTA fund. The client asked our member whether he should stay with that or not. Our member recommended to him, 'Why not?' It is a good performing fund and he should stay in it. There was no need for him to change. The attitude is not one of any prejudice against an industry fund or a corporate fund. It is the fact that some of those funds just do not open themselves up to due diligence that makes it difficult for our members to recommend them.

**Senator BUCKLAND**—And some of those funds do not pay a trailing free.

**Mr Hristodoulidis**—Again, in terms of trail commissions we have researched our membership, and around 75 per cent of our membership offer a choice of fee payment to the clients. It is not an issue of how they pay; it is an issue that the client can choose if they want to pay a fee for service or a commission. It does not enter into the equation.

**CHAIR**—On a point of clarification, this morning all three did not accept trail commissions—it was all up-front fees—and the client had the benefit of any trail commissions that might have occurred. It was credited—

**Mr Hristodoulidis**—To their account.

**CHAIR**—against the fee that was charged.

**Senator BUCKLAND**—How do you see the introduction of portability without choice?

**Mr Hristodoulidis**—Our preference would be that they both be introduced at the same time. As I previously said to Senator Cherry, I do not think you can have one without the other.

**Senator BUCKLAND**—From your point of view, what are the overall benefits to fund members if they change their fund and perhaps chase the best buck they can get? What benefit is there to them?

**Mr Hristodoulidis**—What portability brings to them is the ability to consolidate funds, and there are obvious benefits that flow from one fund with a large amount of money, compared with three or four funds with smaller amounts of money, in terms of the accumulation on it. I believe the benefits of consolidation are quite powerful and quite strong in terms of the end benefit that the client will receive in retirement incomes. The other benefit of consolidation is also for the industry: if the industry are running fewer funds, their costs should come down and that should then be reflected in lower administration costs that the consumers are required to pay back. I think there are two main benefits flowing from portability.

**Senator BUCKLAND**—So would you see benefits in compulsory consolidation?

**Mr Hristodoulidis**—No, I do not think there are benefits in compulsion. I think there needs to be that element of choice for the consumer. I have not had the opportunity to think about it, but there may be circumstances where the client may be better off having two funds rather than one fund. I obviously would need to take that away and consider in what circumstances that might be. But potentially there could be that outcome, so I do not think we should restrict or enforce consolidation.

**Senator BUCKLAND**—Do you think there should be restrictions on the number of transactions per year?

**Mr Hristodoulidis**—Yes. In our submission to the Treasurer we said two per year, but the chair did read out the regulations earlier and there is one. We believe it is important that they have a restriction on the amount of transactions.

**Senator BUCKLAND**—On the disclosure of information at the point of transferring from one fund to another, how far do think you should go with disclosing the cost benefits?

**Mr Hristodoulidis**—We fully support the ASIC policy statement on churning that came out about a month or so ago. Also, as part of our rules of professional conduct, we have the high hurdle of having to show the net benefit of any switching. That has to be in writing and it has to be clearly articulated to the client. We do not believe that any switching should occur without that justification being shown.

**Senator BUCKLAND**—You just said that it should, overall, bring down the cost of administration et cetera. Do you think, on the other hand, that the fees and charges in those funds, particularly industry funds, which would suffer or whose circumstances would change if there were people moving out of them would increase because they have a smaller base?

**Mr Hristodoulidis**—No. We believe that, under both the choice and the portability regimes, the industry funds would be the big winners. They have the lower fee structure; therefore, they should have the flow of income coming towards them. That is purely based on fees and you have to look at other aspects of the investment. But, if you look at it purely on a fee basis, if the

industry funds are the cheapest funds in the marketplace, they should have an influx of new members.

**CHAIR**—Thank you very much for that presentation.

[4.06 p.m.]

**GILLIES, Mr Kash, Secretary, Society of Superannuants**

**WOODS, Captain Ian, President, Society of Superannuants**

**CHAIR**—Welcome. Captain Woods, I am not sure if the committee advised you, but a number of regulatory changes were introduced yesterday that you might not have been aware of. I do not think they impact on your submission, but I thought I should draw your attention to the fact that there have been some changes. They are certainly changes that improve the portability arrangements. Do you have anything to add about the capacity in which you appear before the committee today?

**Mr Gillies**—I am also the spokesman on superannuation for the Australian Licensed Aircraft Engineers Association.

**CHAIR**—We invite you to speak to your submission. We have it before us and we have read it. I was quite surprised that it does not have a reference to the problems of surcharges associated with portability. I thought that was a great oversight on your part!

**Capt. Woods**—I thank the committee for its understanding and for its remembrance of the previous times that we have been here to talk with you. It is nice to come and talk about something other than surcharges because, as much as we would like to get them fixed—

**CHAIR**—I can assure you it is still an issue under portability.

**Capt. Woods**—It is good to know that it has not gone away. I guess there are other issues concerning people that we represent, like Kash's engineers. We come across portability mainly through the aviation industry and the Qantas fund, but there are some aspects of it that we have written about in our submission that we would like to take a few minutes to speak to now, and we will then make ourselves available for any questions the committee may have.

In a general sense, we see portability as complementary to choice. We were supporters of choice—albeit choice with some restrictions—when that inquiry was held, and I guess portability is a step in the direction to give effect to that. As a little bit of general background, many economists would readily admit that our capitalist economy is driven by efficiency; consumers have sovereignty, and if you are to maximise efficiency in any industry, be it aviation or superannuation, then you must have effective competition. That would mean competition on both the supply and demand sides. I have heard organisations like the Australian Consumer's Association say in the past that they believe that there is good competition on the supply side, but without portability and choice the demand side competition is lacking and we do not have the most efficient, sustainable outcome that we could possibly have from the consumers' point of view.

Having said that, we acknowledge that a certain amount of choice and portability is already in practice in the community: members of public offer funds are able to exercise, at their discretion,

both portability and choice. In the industry fund the sponsoring union is able to give effect to choice and/or portability should it so desire. The same goes for corporate funds. Some corporates, like Virgin Airlines, already have choice whereby their members' funds are put to a clearing house and that clearing house sends them to the superannuation fund of the individual member's choice. So we are already part of the way there. Albeit it is not guided by legislation at the moment, it is being practised by certain segments of the superannuation industry.

One of the issues that our society has spoken about and its members are concerned about is that we have a relatively mature situation at the moment where we have market competition in the public offer funds, we have industry funds for some but not all representative groups, and we have a number of corporate funds. As we see it, the situation that the government is driving will mean that corporate funds are going to be faced with a decision in the not too distant future: are they going to compete with market choice and choice of fund or are they going to outsource their superannuation obligations? We would like to put to the committee that, before the corporates are required to make that decision and before the superannuants are put out in the marketplace to make what could be called an uninformed decision, the representative industrial associations should be given an opportunity in the legislation to negotiate with the large corporate funds in order to allow those corporates and their representative bodies to build new industry funds that provide economies of scale, the same as the corporates do, before individual superannuants would go out. At the moment a not-for-profit fund has a cost structure which is much less than that of the competing public offer fund, albeit that the public offer funds have facilities that corporates have not been persuaded to provide as yet. So the point there is that we would like to see industrial bodies afforded the time to carry out these negotiations, and to be empowered to carry them out, before a corporate simply says, 'We no longer want to be part of superannuation. Go out there and do your own thing.'

In a more microeconomic sense, fees are important to both providers of superannuation and the members, and it is always a struggle as to who is going to pay them. If Senator Sherry were here, I am sure he would agree that there is a difference between having penalty entry and exit fees and having entry and exit fees that reflect the true cost associated with the provider of taking people in and letting them exit. If people are going to be churned through a system, somebody must pay the cost. Should it be the people who are currently in the fund? If so, that could be considered unfair by them. Should it be the people who are coming or the people who are going? All we would say is that we are not against fees per se, other than that they should not be penalty fees for profit; they should be fees that truly reflect the cost of taking a member in and letting them exit before normal commercial practice would have allowed the fund to make its return.

The issue of disclosure and education has been well versed in choice, and many of the things that are applicable to choice are also applicable to portability. I do not think I have read anywhere whether anyone has actually asked the Commonwealth whether they are prepared to assist funds and members in the education process in a more direct manner by affording funds a 'subsidy'—for want of a better word—on a per head basis. Those funds could use it to either educate the members or at least educate their representative trustees or their union representatives. 'Unions' is not a dirty word. There is a lot of trust out there and in a complex situation—and I can speak specifically for pilots and I am sure Kash would speak for engineers in the same vein—if something like choice and portability is to go forward and be implemented with confidence by consumers, then unions are an important conduit to be able to transfer the

trust from those that have the intimate knowledge to those that simply rely on personal contacts—'Yes, I believe in that man. If he says it is good for us, even though we don't fully understand it, we have sufficient faith in him to be able to make a decision.' I think that is not as well understood in Pitt Street as it ought to be, but I am sure that unions have an essential role to play to progress the needs of the superannuants and to bring about efficiencies. If they are not adequately included, I do not think the eventual outcome will be as good as it could otherwise be.

So that means that disclosure—as no doubt every submission you have received would say—has to be absolute. People like to obfuscate around disclosure, and, no matter how strong the legislation, it still falls on somebody to call forth behaviour that is in strict compliance with the legislation. I do not know how the government gives effect to something like that except by making a few prime examples out of those who do not disclose what they ought to. Protection comes from empowering the member through education. Hence the need for the involvement of representative bodies, and hopefully a subsidy of some kind because it does take time and money—which is all too easy to spend and all too hard to get. On the savings side, if government could encourage discretionary expenditure in superannuation by building faith in superannuation products then there would be a longer term saving in that there would be more self-funded retirees rather than retirees who do not make discretionary contributions to superannuation and are dependent upon the government pension system. So I would not say that expenditure on education is lost money. Although there is no immediate return, I believe there will be a return in the long run because we will have more people who are independent of the government's pension scheme.

In closing, we think that portability is happening. History would suggest that members need to be protected by legislation. I come back to the old chestnut of surcharge tax: had we been able to persuade the legislature in the initial discussions about surcharge tax, I believe it is a prime example where we could have extended the protection afforded to the public sector funds to the private sector funds—and I thank you for your previous findings supporting the capping. This has pointed out that legislation is necessary for consumers. There is a greater symmetry of knowledge between those that work in the industry and those that are beneficiaries of this industry just by the nature of its complexity. Legislation for portability that is consumer sensitive is an opportunity for government to manage what is already happening as a commercial process but manage it in a way which enhances consumer acceptance and investment in superannuation rather than in the way we feel is happening at the moment where people are losing faith. I read this week that voluntary contributions to superannuation are down 12 per cent in the discretionary area in the March quarter. Whether that is a symptom of poor investment returns or whether people are losing confidence in the system because of its complexity I guess is a debate in itself. We would like to see portability introduced concurrently with choice. I think that to politically withhold one is to deny what is the reality in market practice at the moment.

**Senator CHERRY**—I am a little confused. You say in your submission that you think choice and portability are complementary but you said in your opening submission just then that portability is the first step towards choice. Other witnesses have suggested that choice and portability should be introduced together, but that portability should not be introduced without choice. What would be your view on that?

**Capt. Woods**—The reality is that both of them are happening at this time. If the government were persuaded to introduce either, I think it would be essential, from the consumers point of view, that the decision be made at the same time so that they could both be introduced together. What is there to be gained by introducing either choice first or portability first? The resultant confusion is already out there, and I do not think that confusion is going to decrease. If we had portability then people who have unpreserved, unrestricted components in a corporate scheme like ours might be persuaded by a financial planner to take those contributions out, pay the tax and get rid of their home loan. That will only be half of the story. So I do not see that introducing one before the other is a good idea, especially if we expect to have them both in existence shortly.

**CHAIR**—Under FSR there are real penalties on financial planners who undertake that sort of approach without giving a complete picture. They risk losing their licence to operate if they go down that line. The rules under FSR are very tight.

**Capt. Woods**—It is pleasing to know that the rules are tight. I would reiterate my comment that a few prime examples to make sure people comply with them might not be a bad thing!

**CHAIR**—That might take time!

**Senator BUCKLAND**—You made comment on the situation at Virgin. I am aware of that but I am really not too sure how it is all done. I understand that they put the money in and it is farmed out. I imagine that you have friends and acquaintances within the Virgin organisation. Do you know how some of them are performing in comparison to your own fund?

**Capt. Woods**—I am not aware of the performance of the Virgin fund, but I think it is interesting to note that—

**Senator BUCKLAND**—They might not have one. Do they?

**Capt. Woods**—They do. At the moment their default fund, for want of a better term, I think is Sunstate in Queensland. It is an interesting point you raise because many corporate funds are predominantly defined benefit funds and consequently invested in aggressive long-term strategies, whereas with other funds—and one that comes to mind is the meatworkers' fund—it is a bit of a surprise. In the previous financial year that fund earned plus eight per cent when the average was minus five per cent. It shows that empowerment of the members at least to have investment choice can work in their favour. But I do not know how Virgin compares to Qantas. Kash is a trustee of the Qantas fund; he might have more to say on that.

**Mr Gillies**—I can tell you that the Qantas fund's performance was minus 0.9 per cent, but I do not know the performance of Sunstate.

**CHAIR**—Is that for 30 June this year?

**Mr Gillies**—Correct.

**Senator BUCKLAND**—I was just thinking that I will not let my wife read that bit of transcript or she will have me out killing sheep, I think! If portability were introduced singly or with fund choice, do you think that there would be an automatic increase in fees and charges?

**Capt. Woods**—Kash raised this point as we were walking up here to meet with you. I think we settled on the view that, initially, the difference between not for profit and public offer is the profit maximisation factor. If people simply left either the industry scheme or the corporate scheme and they went to the public offer sector then initially there would be an increase in fees and charges, but I think most economists would agree that eventually you will reach a maximum point of efficiency. Even though it may take some time to move from where we are today, eventually the fees and charges for both the corporate industry and public offer sector will be very close because, although fees and charges in the public offer area would on average be higher than the not-for-profit areas, their member services are also much better. If the not for profit were to add on member services, their costs would have to rise. I would think, like all competitive things, over a period of time we would close that gap from where it is right now.

**Senator BUCKLAND**—Both of you are from very professional organisations, and one of the things—to my knowledge and I hope I am right—is that maths and science are very big subjects for you both.

**Capt. Woods**—That is true.

**Mr Gillies**—Correct.

**Senator BUCKLAND**—Given that, do you think the members of your funds are sufficiently knowledgeable about the workings of superannuation funds to make a very real choice?

**Capt. Woods**—It would be good if we could both answer that because I am sure Kash has a view too.

**Mr Gillies**—I do not believe they are. I can speak with some knowledge about the Qantas fund. It has six primary divisions, some of which are defined benefit and some of which are accumulation. When the members approach me with questions, invariably they do not know which division they are in. When I find out what division they are in, they do not know the difference between an accumulation fund and a defined benefit fund. The reality is that there is not a great deal of knowledge among the members about the workings of superannuation, particularly in the ages between 20 and 40. To state the obvious: as people approach retirement, their knowledge of superannuation increases exponentially.

**Senator BUCKLAND**—Even mine has.

**Mr Gillies**—But they have very little knowledge in their younger years. I also remind the committee that their employers contribute nine per cent and the government provides subsidies. It would be a shame to see their funds diminished, between the ages of 20 and 40, by fees and expenses because they are the years when compounding interest will have the greatest effect in retirement. I believe we need to be particularly careful that their retirement funds are used to the best advantage.

**CHAIR**—As a trustee of the Qantas fund, why aren't you demanding more information for your members about the investment benefits, results, opportunities and options that are there? This committee has recently been calling on superannuation funds to be more proactive in providing education advice, and even advice of a financial character, to make sure that people are moving in the right direction in their careers and as they become older. As people approach retirement and their later years, perhaps they should take a more conservative approach to investment strategy as opposed to their early years when growth might be a more appropriate option—if you provide these sorts of options.

This is where funds do have a responsibility not only to collect that money and pay it out as a lump sum if it is in an accumulation scheme but also because this is where people get themselves into trouble. They go into the marketplace, they lose their contact with Qantas or their previous employer, and a lot of them are foundering. They have a big sum of money—the newspapers, I am told, say that people want that lump sum intact so they can spend it as they like. We believe that, if you go down that line, it is a very expensive savings bank. After all, if employers are going to put money away for retirement, it should be for retirement and not for paying off debt as a result of a failed investment scheme that you might have had along the way.

**Capt. Woods**—Are you implying a change from a lump sum to a pension kind of arrangement?

**CHAIR**—In the last majority report, we said that in the longer term it is desirable to look to a system in which some portion of the lump sum goes into income stream products. We called on the government to make them more attractive through legislative changes because the market is very restrictive and not very attractive at the moment. After all, people surely want an income in retirement.

**Capt. Woods**—They do. I will just add something in response to Senator Buckland's question. Pilots are a little bit different. It is worth noting that you have a group that is electronically connected, for whatever reason, and is using electronic communications daily—and I have noticed this in the surcharge petitions we are collecting. We collect them from Kash's engineers and from my pilots. Inevitably, Kash's engineers send in theirs in an envelope or by fax machine; the pilots just sign the electronic thing on the web site. To answer your question about educating people, there is not one answer; there is not one size fits all. I would not say it is socioeconomically driven. People in an industry who are computer familiar and use a computer every day will be much easier to educate, to give information and to get information from than people whose workplace does not put them in contact with a computer.

Certainly, as a pilots association, one of the reasons we have proposed a fund—we would have no problem in bringing in engineers—is that when we say to some corporates, 'We want to provide education; we want to empower the membership,' they say, 'We have 30,000 members and we reckon that only 10 per cent are going to use it. It is okay for you blokes because you have an average account balance of 300,000 and our average account balance is 10,000, and we find that those people don't use it, so you can't have it.' Again, one size does not fit all.

It is more important that those who have the wherewithal to be independent of the government support system in retirement understand how to optimise that independence, and that is sufficient reason to educate them. If they run foul of the system, somebody who should have been

independent of the system becomes yet another person who will be supported by the community who otherwise would have been able to stand on their own two feet. I have here a transcript of what we spoke to, just to clarify some points.

**CHAIR**—Thank you very much for your interesting presentation, as usual.

**Capt. Woods**—It is good that the people whom we represent feel that they can talk to people they work with who can cut out some of the filtering that takes place. I am sure that Kash will be inundated with people who want to know your views. It makes the system work. Thank you for inviting us.

**CHAIR**—We need a resolution. The committee will form a subcommittee for the hearings in Melbourne tomorrow, 1 August. As part of its inquiry into portability of superannuation, the subcommittee consists of any two of Senator Watson, Senator Cherry and Senator Buckland. Is that so resolved? It is so resolved.

**Committee adjourned at 4.33 p.m.**