



COMMONWEALTH OF AUSTRALIA

# Official Committee Hansard

## SENATE

SELECT COMMITTEE ON SUPERANNUATION

**Reference: Portability of superannuation**

FRIDAY, 1 AUGUST 2003

MELBOURNE

BY AUTHORITY OF THE SENATE

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

**Friday, 1 August 2003**

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

**Senators in attendance:** Senators Buckland, Cherry 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 9.03 a.m.****SILK, Mr Ian, Convenor, Industry Funds Forum**

**CHAIR**—Welcome. I declare open this second public hearing of the Senate Select Committee on Superannuation as part of our inquiry into portability of superannuation. Under its terms of reference, the committee's inquiry will focus 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; and (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. Today, the committee will hear evidence from a range of individuals representing the following parties: the IFF, Superpartners, Cbus, Mercer Human Resource Consulting, the Corporate Super Association, the IAA, the ACTU and CPA Australia.

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 broader 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 you wish to discuss with the committee in private, we will consider your request.

It is a privilege this morning to hear from Mr Ian Silk, and I invite you to make an opening statement. We apologise for the inconvenience caused to you as a result of the government's introduction of some further amendments to portability which may have affected your submission.

**Mr Silk**—Thank you. I am aware of the regulations that were released yesterday. I should preface my comments today by saying I only received them late yesterday. I have not had a chance to consider them as fully as I would have liked, and I certainly have not had the opportunity to speak to other members of the Industry Funds Forum about them. So my comments are qualified to that extent.

**CHAIR**—I mentioned that because it may even change the approach of some witnesses to the portability issue in terms of the stand that they have taken previously.

**Mr Silk**—Yes. The Industry Funds Forum represents around four million members in around 24 large industry superannuation funds. We have several hundred thousand participating employers and over \$30 billion in assets. We appreciate the opportunity to appear before the committee today and make our submission, which complements the written submission that we provided to Treasury late last year and the written submission we provided to this committee last month.

As we have previously stated to this committee, the Industry Funds Forum supports the operation of a superannuation system that provides members with safe, wealth-generating, efficient and member focused superannuation services. Such a system, underpinned as it is by legislatively mandated employer contributions, requires a regulatory regime that takes account of sound public policy considerations and the best interests of members.

The delay in introducing a choice of superannuation funds system as proposed by the government over recent years is due in part to disagreement over the details of an appropriate regulatory regime. The Industry Funds Forum supports choice of fund provided that the regulatory regime that underpins such a system is comprehensive and effectively serves the interests of members of superannuation funds rather than serving the interests of the providers of superannuation services.

The essential elements of such a regulatory regime as previously submitted by the Industry Funds Forum include an effective and standard disclosure framework, a ban on commission based selling of mandated superannuation contributions and a comprehensive public education campaign around the issues that members should consider when contemplating transferring between superannuation funds.

As to portability, the Industry Funds Forum is a very strong supporter of a system that facilitates the speedy and inexpensive consolidation of superannuation accounts into a member's active account. If measures were introduced to increase the efficiency with which this occurred, this would represent a substantial improvement in the Australian superannuation system. However, the portability proposals as originally drafted and as gazetted yesterday extend way beyond this positive objective. The portability proposals as reflected in the regulations would effectively implement the government's choice of fund proposal, albeit confined to previous contributions rather than for future contributions.

Apart from whether it is appropriate for the will of the parliament, as reflected in the failure of the Senate to pass the choice of fund legislation, to arguably be attempted to be subverted by the gazetting of these regulations, the Industry Funds Forum believes that it would represent bad public policy for the regulations to become operational. If these portability regulations were to proceed, the same regulatory regime that we have advocated under a choice of superannuation fund system—that is, a ban on commissions and compulsory contributions, common disclosure requirements and a public education campaign—should form part of these regulations.

However, and more fundamentally, the portability provisions and the choice of fund provisions should be considered together as part of the same package. They both relate to the circumstances in which a member can transfer their superannuation from one fund to another. It is quite absurd, in our submission, to have the regulatory provisions governing the transfer of previous contributions to be different from those governing the transfer of future contributions. However, if we are to look at the issue of portability of previous contributions in isolation from that of future contributions, the Industry Funds Forum is most concerned about how the regulations might operate in practice.

Almost all of the stakeholders that our member funds have spoken to and with whom we have discussed our understanding that the provisions would allow regular and modest transfers to occur were originally horrified at the cost and resource implications of such arrangements. We are conscious that some of those issues have been addressed in the regulations that were released yesterday, and we will make some comments on those changes. Whilst, as I said at the outset, we have not been able to properly consider the new regulations, we do have some comments to make about the changes.

The two major changes that we understand to have been made in the regulations gazetted yesterday from those originally released are, firstly, a limit on the number of such transfers to one per year; and, secondly, a requirement for a minimum of \$5,000 to be retained in the member's account if a member chooses to transfer part of their account to another fund. In relation to the first issue—that is, a limit on the number of transfers to one per year—we submit that that is a significant improvement on the proposals contained in the original regulations. However, that is an improvement from a very low base. The original proposal—and we need not now go into the details—was fundamentally flawed and would have caused significant long-term damage to the retirement incomes of a number of Australians. It would have imposed significant additional cost pressures on the system as a whole that would have ultimately been borne by the members of superannuation funds.

The change to a limit of one per year is an improvement, but represents an incremental improvement rather than a fundamental beneficial change to the regulations as originally proposed. That change does not address the fact that the regulations overall still represent choice of fund without the safeguards that we say should go with such a system. Perhaps most fundamentally of all it does not address the real issues that serve to block portability in the system, and we will come to address those in a moment.

The second change to require a minimum of \$5,000 to be retained in a member's account is again a change for the better but, as in the first instance, does not represent in our view such a significant change as to see the package contained in these regulations as being an overall improvement to the system. Aside from family law considerations, the requirement for a \$5,000 minimum account balance to be retained would serve to protect the member benefit protection interests of the fund from which the transfer was occurring albeit, depending on the amount of money transferred out of the fund, member benefit protection costs may still be incurred by the fund into which the money is to be transferred.

One of the principal objectives of these regulations was, in our understanding, to see a reduction in the number of superannuation accounts in Australia, and that is an objective that we strongly support. As this committee is aware, there are nearly three superannuation accounts for every working Australian. That is an entirely undesirable outcome of the system we have. However, it is our very strong belief that, if these regulations were to become operational, far from achieving the objective of reducing the number of superannuation accounts in the country, the almost certain outcome would be the polar opposite of that objective—that is, we believe these regulations will lead to a proliferation of superannuation accounts. They will not lead to the status quo in the number of superannuation accounts and they certainly will not lead to a reduction. There will almost certainly be an increase in the number of superannuation accounts.

We think it is appropriate to consider how the superannuation system is currently operating and what the actual blockages to movement of accounts are—in particular, what are the actual blockages to account consolidation. As noted in our written submission, we see there being three major blockages to account consolidation: firstly, the imposition by some funds of excessive exit fees and penalties on members as they seek to transfer out of funds; secondly, deliberate delays in the implementation of a member's request to transfer their account from one fund to another; and, thirdly, member apathy in consolidating old superannuation accounts into new accounts established with new employers.

The regulations do seek to address the second of those issues—that is, deliberate delays imposed by a superannuation fund in implementing a member's request to transfer out. As the committee would be aware, the regulations impose a maximum time period of 90 days—from the receipt of a properly documented request—by which the transfer must be implemented. We believe that is an improvement on the current provisions, in that there is no currently imposed maximum time period by which such transfers must be implemented. Therefore, we support the introduction of the 90-day period.

We would go one step further and suggest that a shorter period of time would be entirely appropriate. We believe that a 30- or 45-day period would still give superannuation funds sufficient time to act on a request following receipt of appropriate documentation. Indeed, many industry funds have business rules with their administrators that require properly documented transfer requests to be actioned within five days. A 90-day period is a very comfortable period of time for all superannuation funds to act upon such requests. As I have said, the Industry Funds Forum would be very comfortable with a shorter period of time—say, 30 or 45 days.

The third issue that I mentioned was member apathy. We believe that is best addressed by public education and information campaigns, rather than it being something that can be properly addressed through regulations or legislation. Indeed, the committee would be aware that last year many industry stakeholders, including CMSF, the Australian Taxation Office, the Australian Preservation Fund and a number of industry superannuation funds, conducted a campaign around 'Lost Member Week', which sought to consolidate a large number of superannuation accounts. That campaign was particularly successful.

However, there are practical constraints that I have identified on account consolidation that may well benefit from regulatory change. They are to date not picked up in the regulations. One of the largest inhibitors to account consolidation is the excessive exit fees and penalties that are charged by some superannuation providers when their members seek to transfer their accounts to another fund. As noted in the IFF written submission to the committee, some exit fees and penalties represent an outrageously high proportion of a member's account balance. The negative elements of this issue are compounded when it is considered that most of the savings in these accounts are comprised of employer contributions mandated by the federal parliament through the SIS legislation.

I understand that at yesterday's hearings before the committee the IFSA representatives argued that the sorts of examples noted in the Industry Funds Forum submission were most unusual and were effectively aberrations. Regrettably, this is simply wrong. These examples were obtained from Industry Funds Financial Practice, which is an organisation which provides financial planning advice to members of a large number of industry superannuation funds. Industry Funds Financial Practice sees approximately 2,500 members each year. In fact, it sees a higher number of members, but it sees around 2,500 members who come to them seeking advice in relation to transferring from one fund to another.

The advice from Industry Funds Financial Practice is that approximately 30 per cent of those people seeking advice about transferring from one fund to another receive advice from that organisation to the effect that they should not implement such a transfer. So we have got two sorts of people here: people who have come to Industry Funds Financial Practice having decided themselves that they wish to transfer and seeking either confirmation of that or some practical

assistance to give effect to that decision; or they are people who have come seeking advice and one of the issues on the agenda is whether they will transfer. In fully 30 per cent of such cases they are advised not to transfer because of the excessive fees and penalties that they would incur if such a transfer was to take place.

The written submission that Industry Funds Forum provided gave five examples of fees ranging from 19 per cent to 95 per cent, the 95 per cent example being a person who has an account balance of \$5,939.14 and had they transferred they would have forfeited \$5,621.11—a 95 per cent penalty. At the other extreme of those examples is a 19 per cent penalty where a person with an account balance of \$216,705.36 would have paid \$40,595.40 for the privilege of transferring out of that fund. These are not issues where the fund is refusing to implement a member's request to transfer. They are not refusing it in the sense that they are making an absolute denial of the request, but they are effectively refusing an intelligent person the right to transfer because nobody in their right mind would incur those penalties. So the funds are saying, 'By all means take your money out,' but as they walk out the door the fund is sticking its hand into their pocket and pulling out a huge amount of the account.

**Senator CHERRY**—We have heard from other witnesses that the incidence of these sorts of fees has been declining quite rapidly and they are older style funds. Would you agree with that assessment?

**Mr Silk**—I understood that was put to the committee yesterday. In fact, I contacted Industry Funds Financial Practice this morning before this hearing to put that to them. They said that is certainly not the case. Certainly endowment policies are reducing as a proportion of policies in the community, but many of the instances that I have spoken of—and I have got pages of other examples here with similar amounts of money and similar percentage fees—are from modern day master trusts by many very well-known providers of master trust products. So, first, it is not a small problem. Second, it is not confined to endowment type policies. Third, it is a feature of large master trust products that are promoted by many of the industry's biggest players.

**CHAIR**—Would you like to table that information?

**Mr Silk**—I would be happy to do that. Indeed, I would be happy, if the committee wished, to provide more detailed information about that.

**CHAIR**—We would like that, because we were challenged yesterday. As chair I took up some of those large costs of exit with one of the witnesses, who challenged the committee and asked the committee to provide evidence to support that allegation. So if you could help the committee it would be appreciated.

**Mr Silk**—I am happy to do that.

**CHAIR**—In the interests of full and fair debate.

**Mr Silk**—Yes.

**CHAIR**—Of course, we would not want people's names associated with that in terms of the individual involved.

**Mr Silk**—No, and the material that I have provided today and the material I will provide subsequently does not include members' names.

**CHAIR**—We have to respect the privacy provisions.

**Mr Silk**—That is right. In the sorts of cases we have discussed, where members would incur excessive exit fees and penalties, many members choose not to proceed with such a transfer. Thus such fees and penalties are a clear and significant constraint to account consolidation and portability in the industry. If these regulations sought to address that issue, which is a real and practical constraint on account consolidation and portability, one way of doing so would be to impose a maximum penalty on a member's account if they were to transfer from one fund to another. We would suggest that a fee in the order of \$50 would be an appropriate maximum.

**CHAIR**—How do you overcome a contractual obligation that has already been undertaken, though?

**Mr Silk**—I think there are two issues there. One is contractual obligations in relation to contracts that exist today, and there would need to be some transition provisions to take account of those. But, more fundamentally, we submit, as I have indicated in our written submission and also have said today, that there should not be commissions—which is the major issue at play in terms of contracts—on mandated employer contributions. If the federal parliament dictates that employers should pay nine per cent of an employee's wage or salary into a superannuation account then we say it is entirely inappropriate for third parties to excessively enrich themselves at the expense of the intended beneficiary of those payments. The sorts of examples we have spoken about today can only be seen in the context of excessive enrichment of third parties on the one hand and a corresponding diminution in the benefit that should have been received by the beneficiary of the payment on the other hand.

In relation to the issue of superannuation funds delaying the transfer of a member's account to another fund, industry funds have had some experience of non-industry funds apparently doing just that. This is clearly inappropriate behaviour on the part of any superannuation fund. The provision in the draft regulations requiring that a request be answered within 90 days is a welcome and positive initiative. As I noted earlier, we welcome that initiative and indeed would be happy to see that 90-day period reduced to 30 days or 45 days. As I noted, many industry funds act on such requests within five days, so a 30-day or 45-day period should be achievable by any superannuation fund and its administrator.

In conclusion, the Industry Funds Forum supports the portability of superannuation accounts—that involves the removal of obstacles that prevent the consolidation of inactive accounts into active accounts. To this end, the Industry Funds Forum supports: (1) a limit on exit fees and penalties to, say, \$50; (2) development of an industry wide protocol concerning the information required to process a transfer request; and (3) a maximum processing period of 30 days or 45 days. I should just note in relation to the industry wide protocol proposal that there are sometimes delays in giving effect to a member's request to transfer, because a particular fund may say that a member has not provided sufficient information, and many funds have their own requirements. We submit that if an industry wide protocol were developed that had the support of all major players, there would be one set of information requirements that would apply—

**CHAIR**—Sorry about that interlude. Those bells made it impossible to continue.

**Mr Silk**—That is okay. I am not quite sure where I was at.

**Senator CHERRY**—You were concluding!

**Mr Silk**—Yes, I was in the middle of concluding. Perhaps I can go back to the three points I was making. The Industry Funds Forum supports a limit on exit fees and penalties of, say, \$50; the development of an industry wide protocol concerning the information required to process a transfer request; and a maximum processing period of 30 or 45 days, noting that the 90 days currently proposed is an improvement on the current provisions. We would submit that each of those provisions would make a substantial practical improvement on the current provisions that serve to inhibit portability and consolidation of accounts.

However, if the portability provisions are to extend beyond consolidation of inactive accounts into active accounts, this should be considered together with the choice of fund provisions. When considered jointly, the accompanying regulatory regime should protect the interests of members by (1) banning commissions on mandated contributions, (2) enforcing an effective and standard disclosure framework and (3) instituting a public education campaign based on the issues to be considered when transferring between funds. The Industry Funds Forum appreciates the opportunity to appear before the committee today. I would be happy to answer any further questions.

**CHAIR**—Concerning exit fees, in the absence of a legislative cap, do you not believe that an unintended consequence for funds to protect the amount under investment would lead to an increase in exit fees, rather than a decrease, through the force of competition?

**Mr Silk**—I am sorry?

**CHAIR**—Unless we capped exit fees, we might see an increase in the amount of exit fees as funds tended to protect the investment.

**Mr Silk**—There is no question that that would occur. For example, there is a number of industry funds that do not charge exit fees at all. Some funds charge a modest exit fee; others do not charge an exit fee and costs associated with processing exits are absorbed within the base administration fee. But the outworkings of these regulations would certainly see an increase in activity of members transferring between funds, therefore an increase in the number of exits. The very great likelihood is that, even on a simple cost-recovery basis, many of the funds which currently do not charge an exit fee would have to introduce one. I think your question was directed to the preservation of assets and what funds might do in that regard, and I would have thought that is a logical approach that some funds might take—logical in the sense that they want to preserve assets. If you put that to one side and just look at those funds that want to act purely in the interests of their members and simply want to recover expended costs, we will see an increase in exit fees in some instances and certainly the introduction of exit fees where currently they do not exist.

**CHAIR**—Concerning surcharge, where there are outstanding obligations but the tax advice has not yet been received, will there need to be some protocols? We could see a number of

transfers of funds because the tax office are often a couple of years behind in issuing surcharge obligations.

**Mr Silk**—Yes, they are. That is one instance but there are many where the transfer of a benefit does not occur neatly and on one occasion; rather it can be staggered over a period, depending on what the issue is. Again, that is an instance where the imposition of an exit fee or an increased exit fee will serve to reduce the money that is ultimately paid to a superannuation beneficiary or to an account holder.

**CHAIR**—Can you articulate why you believe there would be an increase in the number of accounts under a portability regime?

**Mr Silk**—If portability is introduced in the absence of choice of fund, as is currently contemplated, we will have instances where an employer is making a payment into fund A and the employee of that employer will come along to fund A and seek to transfer some or all of that employer payment into fund B.

If fund B happens already to have an account under that employee's name, the best case scenario is that there will be no change in the number of superannuation accounts, because the employer will be continuing to make payments into fund A. So that account will remain or will be reopened upon the next employer payment into fund A, and fund B will exist. That is the best case scenario—that is, no change in the number of accounts, certainly not a reduction in the number of accounts. It is impossible to conceive that every member with payments going to fund A will be transferring into an existing account. The very great likelihood is that, on a proportion of those occasions—and none of us knows what that proportion might be—they will be transferring out of fund A into a new account; that is, they will establish a new account elsewhere. In that eventuality, there will be an increase in the number of superannuation accounts. But, in our view, the model of portability as proposed in these regulations cannot and will not lead to a reduction in the number of accounts.

**Senator BUCKLAND**—Looking at the figures we have been provided with—and I had already done some calculations on the figures that were in your submission, for which I thank you because it is extremely valuable to the work of the committee—I am just trying to do a rough calculation now, and it appears to me that the smaller balances are the ones that are attracting the higher fees. I am wondering whether the percentage numbers on the right-hand side of the column are consistent throughout the period in which a person has money in a fund or whether the fee varies with the size of the account.

**Mr Silk**—There are a number of variables that go into the calculation of the fee, but I think that the best approach is in the supplementary material that I have obtained from Industry Funds' financial practice. I will get them to address that issue and seek to provide the committee with information as to those elements that go to constituting whatever the exit fee or penalty is.

**Senator BUCKLAND**—I am disturbed by the number of exit fees that are in excess of 50 per cent. Looking down the list, I see that you have someone with \$1,299 paying \$792 to exit, and there is one you have already highlighted with 94 per cent. I was looking out of pure interest, because I wanted to transfer some money that I had in a fund when I left my former

employment. I see that it attracts 20.3 per cent. It is certainly enough for me to say that it will just have to stay there and suffer the losses it sees at the moment.

**Mr Silk**—Most industry superannuation funds encourage members to consolidate their accounts. But it is a mark of the unsatisfactory state of the industry in relation to this particular point that most industry funds, in their literature encouraging members to consolidate their accounts, have to urge members to check what the exit fee or exit penalty would be were they to transfer. So one of the first issues to consider is what it is going to cost you for the privilege of transferring out of a superannuation fund that you would otherwise automatically choose to transfer from.

**Senator BUCKLAND**—The whole thing that those figures highlight very clearly for me—and, to be honest, they are very distressing—is that the most vulnerable—those in the lower paid jobs with the lower amounts of savings—are again the ones who are going to suffer the most. That is terribly distressing, something that needs to be made a lot of. I will leave it at that. I was going to ask, in relation to your submission, about people wanting to move their funds. This is not about those who, like me, want to consolidate into one account—and my son wants to do the same with the three funds that he is necessarily in—but those who seek to move their money to look for better earnings. From your experience of your fund members, are they more likely to be itinerant workers or workers who are in stable factory or company jobs?

**Mr Silk**—Are you talking about people who would like to exit from a fund altogether and move to an entirely separate fund?

**Senator BUCKLAND**—Yes, and they are trying to get a little bit more than what they are getting now.

**Mr Silk**—It is a bit difficult to respond in a blanket fashion in a way that would cover the majority of people, but you raise an interesting point from this perspective: the portability debate has arguments to the effect that this will facilitate people being able to do precisely what you have said, when in fact that is not necessarily the case because it is confined to contributions that have already been made, not necessarily to prospective contributions. That is why we say that, if there is going to be the introduction of mechanisms to address previously paid contributions, it should go hand-in-hand with provisions that address future contributions—and that of course relates to choice of fund. There is not in fact the great constraints that some people suggest on people seeking to change the fund that would be the repository of future contributions, as the system has been freed up. There has been far more flexibility within the industrial relations and superannuation systems over the last six or eight years, and the number of complaints that exist in the superannuation system as a whole, about members' inability to transfer from a poor performing fund to a superior performing fund, is absolutely minimal, and that is across the whole system. So we come back to what are the real problems, the real constraints, in the system today that are inhibiting people from consolidating their superannuation. There are three that we have identified: member apathy, excessive exit fees and penalties, and delays imposed by superannuation funds. In our submission, these regulations do not address the real problems in the industry. They seek to address some other issue and they are not targeting the real issues which are inhibiting account consolidation and portability.

**Senator BUCKLAND**—In your submission you mention that if this were introduced costs would increase. It is a view that may be held by some on this side of the table. Do you have any ballpark figure on the increase? I have asked others this and it is a very difficult question to answer. Do you have any views on the extent of the increase that would necessarily be imposed to accommodate this?

**Mr Silk**—No, I cannot really provide anything useful there, I am afraid.

**Senator BUCKLAND**—That is okay. Still on that and without giving figures—because it is a large question and I do not think anyone has really tried to assess the increase yet—would it need to be applied to all members of a fund or only those who are participating in the funds transfer?

**Mr Silk**—That issue would be determined on a fund by fund basis. As I noted before, some industry funds have a transparent exit fee which is a modest amount that covers the cost of giving effect to the transfer. Others do not, and it is absorbed in a base administration fee. The \$5,000 minimum for member benefit protection costs that is contained in the new regulations addresses for the most part the member benefit protection costs for the original fund. But if a member has, for example, \$5,500 in an account and transfers \$500 from fund A to fund B, there may well be member benefit protection costs in fund B to protect the \$500, depending on whether future contributions are made, the administration fees, the investment earnings and so on.

On my first reading, it would appear that the regulations allow a member to transfer an amount out of fund A if it is less than \$5,000. So if the member has \$50 in an account they are able to transfer that out. If the exit fee of that fund is, say, \$80, there will be member benefit protection costs attached to that and they would be borne by the members of fund A. Under the current arrangements, that member could not transfer it, assuming it was an active account and ongoing contributions were being made into it, so that would be a new cost into the system.

**Senator CHERRY**—Your evidence has been helpful to me this morning in my trying to sort out what is broken about portability at the moment, which is one of the issues this committee has grapple with. I was interested in your recommendation of a 45-day maximum period on transfers, which I think is unique among our submissions. Some of the administrators we heard from yesterday suggested that the vast bulk of transfers are done within 30 days but, where they are chasing arrears or there are other issues, that can blow out. How would your 45-day rule impact on those more complicated transfers?

**Mr Silk**—I sought to use the term ‘properly documented requests to transfer’. By that I mean a request to transfer that had all the appropriate information and that the administrator could act upon it. I think there are a few issues here. The regulations properly take account of the sorts of instances you have talked about. There are provisions where, if the appropriate information is not provided to a fund within 90 days, further leeway is provided. We think that is an appropriate principle. That is the first point I would make.

The second point I would make is that, as I noted in our submission, we believe there is scope for the industry to come together to develop an industry-wide protocol on the information that administrators need to implement a transfer. Whilst there are be issues such as arrears payments

that need to be followed up with an employer, for example, there are also delays caused by particular superannuation funds having their own requirements, which often seem to be more about preserving funds under management than about seeking to make a contribution to an efficient and smoothly running superannuation system by giving effect to member transfers. If the industry came together and developed an industry-wide protocol that would be adopted across the board, that information in a consistent documented form could be provided to members whenever they wanted to transfer.

**Senator CHERRY**—But the industry has been talking about an industry protocol for 10 years. What steps do you think we need to engage in to get to an industry transfer protocol?

**Mr Silk**—In the first instance, I think if this committee made a strong recommendation to the industry as a whole and particularised that ASFA and IFSA, for example, should take the lead and convene a meeting of key stakeholders, with a view to developing such a protocol, that would put the responsibility on a couple of the lead organisations in the industry. With the heightened publicity on this issue that is sure to come from this committee's report, I think you might see people really focus their minds on it in a way that has not happened to date.

**CHAIR**—We have run over time, Mr Silk. It was an interesting presentation. Thank you very much. There are no privacy problems; we have checked with the Clerk in terms of incorporating that document.

**Mr Silk**—I will speak with industry fund financial practice and either they or we will provide the further information that I spoke about.

**CHAIR**—There is a deadline of 21 August in terms of our reporting date.

**Mr Silk**—I will give it to you well before then.

**CHAIR**—Thank you.

[9.55 a.m.]

**GALBRAITH, Ms Fiona Anne, Manager, Compliance, Superpartners Pty Ltd**

**CHAIR**—Good morning. We would like you to make an opening explanatory statement.

**Ms Galbraith**—Superpartners is an administration company that administers 15 large and medium sized industry and superannuation funds totalling over four million members and hundreds of thousands of contributing employers. It currently has about \$10 billion of assets under management, so quite a sizeable proportion of the industry. We welcome the opportunity to present to the committee this morning.

The first observation I would like to make is that we were a little surprised by the gazettal of the final regulations yesterday and noted that a number of changes had been made between the draft and the final regulations, changes on which I am only partially up to speed. I will try to refer to the now gazetted regulations where appropriate.

I guess our major submission is that we would prefer to see portability deferred so as to come in at the same time as choice of funds comes in, for reasons similar to those outlined by the previous speaker. There is a logical synergy between the two of them and it is almost impossible to have one working effectively without the other. When choice of funds does come in, it will be a bit of a nonsense to have members who are able to choose where their contributions go but not where their current account goes. Similarly, it could be argued that it is equally a little bit of a nonsense at the moment to have members who can move their account balance around even though they are still receiving contributions into the fund. This will cause us some considerable administration issues going forward.

Our preference, because the two are clearly related and complementary measures, is that they should be introduced simultaneously and not one ahead of the other. Either way around has issues and, as referred to by the previous speaker, would actually lead to more accounts rather than fewer accounts. If your contributions are flowing in one direction and you can move your account in another direction rather than keeping the two together, which is probably the most logical outcome, then that will lead to more accounts not fewer. There are also some administration issues, which I will refer to in a minute, that may end up creating multiple accounts within the same fund.

If introducing them simultaneously is not possible, our second preference is that portability should only apply to a member where that member is no longer receiving contributions into the fund—so where there is some concept of contributions or employment having ceased. Short of choice of funds coming in, that would still be our preferred model, as opposed to the current regulations. That would probably require some kind of measure where, upon receipt of an application to transfer out, provided no contribution had been received for some prior period—say, 90 days—it would be a valid request. If a contribution had been received in some prescribed previous period then it would not be valid. The mechanics would have to be worked out but that is how we would like to see it operate.

We note that probably one of the most material changes to the final regulations from the draft regulations has been the introduction of the 12-month rule. If the regulations are to go forward as gazetted, that will certainly assist in the administration. If it is confined to being once in every 12 months, that certainly makes our life a lot easier.

We assume that the \$5,000 limit is there as an anti-avoidance measure for family law, because under family law \$5,000 is the minimum amount to be split. We assume that the government has introduced that so that people cannot split their accounts into sub-\$5,000 amounts and avoid a family law order. I guess the major issue we have is that because of that rule, which is there for a good reason, people with under \$5,000 will be compelled to take their whole account and a lot of admin systems—mainly for audit trail purposes—have been designed such that if a member takes their entire account balance then they must close their account.

If we have the scenario of members who are receiving ongoing contributions taking their entire account balance every 12 months, we will have to close that member's account and then when the next contribution comes in create a new account for them in the same fund. This causes a number of administration issues for us, the most pertinent being that it is difficult to carry the member's history across. Either it does carry across, in which case it is cluttering up significant amounts of system memory in replicating the same sort of header information in different accounts, or it does not carry across, and that can lead to various issues down the track such as compliance obligations; for example, you can only pay a financial hardship benefit once every 12 months. The system can monitor that against one member, but if you end up paying a financial hardship benefit and then closing the account because of portability and opening up a fresh account, it is going to be difficult for the system to keep track of the fact that that same individual was paid a financial hardship benefit in the previous 12 months because it would actually be a separate account.

Similarly, there might be issues in allocating contributions because an ex-contributor will have the old account number and will have to tell an employer the new account number. So there are all sorts of issues there—even things like carrying across address history, which is something we use a lot to verify the identity of members. If all the address histories does not come across, we may have some issues there. So we submit that you may find there are multiple accounts, even within the same fund, because of the way computer systems are set up in terms of the total withdrawal of benefits from a fund—you usually need to close that account and start a fresh one. If you do not do that, there are also issues with the way systems work in calculating fees, charges and interest properly on accounts which go to zero balance and start again.

Our other observation on the regs as gazetted yesterday is that there are a couple of concessions in there, one of which is the 12-month one; that is, if you have rolled over once under portability regulations in the previous 12 months, another request is not valid. The other concession is that a member who exercises portability is no longer a protected member. We actually think that those concessions are too narrow and need to be extended so that, basically, if a member has rolled out any amount of money in the previous 12 months, irrespective of whether it is done under portability or just generally, they need to cease being a protected member and the 12-month rule needs to start from there. Otherwise we may see the unintended consequence that, if it is better off for the funds, particularly from a protection perspective, for it to be a portability rollover and not a permissive one, they may close down the permissive ones

and only allow portability ones, which is an undesired consequence that will actually narrow portability.

So we think that those two exemptions need to be triggered by any rollover out of the fund not just a portability rollover. The only other observation we would make about the regs as gazetted yesterday is that we found regulation 6.34 (2), which talks about the information that must be given to members, a little of unclear in terms of exactly how that mechanism is meant to work. We suspect it will end up just being a rubber stamp exercise, but we will wait and see. The exclamatory statement was not terribly helpful on that point. That is a new introduction since the draft regs. I guess our major concerns, as referred to by the previous speaker, are the same concerns we have about the introduction of the choice of funds environment. Both face similar issues, two issues mainly: the relative lack of financial literacy of superannuation members and therefore their susceptibility to poor financial advice. Both choosing the fund to receive your future contributions and choosing the fund to transfer your existing benefit to involve the same kinds of considerations about returns, fees, charges and various other issues.

It is basically the same sort of decision that needs to be made and we submit that the necessary precondition before both of these measures come in is that measures be made to improve the financial literacy of Australian superannuation members, improve disclosure and to improve the conduct of financial advisers. I must admit that I have just returned from leave and have not been well so I have not had time to read your most recent report, *Planning for Retirement*, but I did have a quick skim through. I noted that recommended 11 on page 163 was about improving financial education. At the risk of repeating what has probably been said at previous hearings—not so much at this particular inquiry but probably at your previous one on planning for retirement—and looking at the ANZ financial literacy research, one of the most staggering results that leapt off the page at me, and I noted it is repeated in your report, is the fact that 85 per cent of people maintain they understand the risk-return relationship and yet 47 per cent, which is nearly half, would have invested into an investment that promised well above market returns with no risk. That demonstrates that they clearly do not understand the risk-return relationship. ASIC and ANZ drew the conclusion that people were potentially susceptible to misleading claims, which I think is a classic understatement. They clearly are. Misleading claims is really what choice of funds and portability is all about. There will be a potential for funds—and, more likely, intermediaries—to make misleading claims and have people make poor choices in relation to funds, be they about contributions or transfer of benefits. There are two conclusions you can draw from that, one of which is their susceptibility to financial advisers. That can be demonstrated by the ASIC website which has a special web page which they call the ‘Gull Awards’. Every month they feature particular investments that susceptible consumers have been misled into.

**Senator BUCKLAND**—Before you leave can you give us the webpage address for that?

**Ms Galbraith**—I think I probably can give it to you—at least, the ASIC high-level one.

**Senator BUCKLAND**—Thank you.

**Ms Galbraith**—It is quite interesting reading. Each month they feature live examples. It relates to the investment market generally, not just to super. One time in particular they did something themselves. I cannot quite recall the details but it was to the effect of publishing, I

think, on the intranet a totally unregistered scheme. They just manufactured a scheme themselves and there was a staggering response to it because people had not even bothered to go to the ASIC website to verify that it was a registered scheme. So we have some concerns with the level of literacy out there and that is reflected by the results of the ANZ survey. There were some highlights for me when I was reading it last night. Only 51 per cent thought that diversification was very important; and 37 per cent of people—over a third—do not understand that good investments have short-term fluctuations. That is a major concern because if over one third of the population do not understand that good investments have short-term fluctuations, particularly for a long-term investment like superannuation, it may lead to the kind of behaviour—people chasing returns—that Senator Buckland alluded to in questioning the previous speaker. If 37 per cent of people do not understand that a good investment may have short-term fluctuations, it shows that a lot of investors have a short-term view and may be susceptible to chasing short-term returns at the expense of long-term returns.

Of those surveyed, 55 per cent had little understanding of fees, which is a major concern. Only 54 per cent—just over half—of people surveyed understood that superannuation had concessional tax treatments. Considering that even with the surcharge it is still the most concessional investment there is, that is a concern. Only 25 per cent really understood compound interest. A much higher percentage thought they did but on further investigation only 25 per cent did. That means that they are particularly susceptible to not really appreciating the difference that even relatively small differences in returns can make, given the compounding nature of superannuation and that it is a long-term investment. So they would be susceptible to somebody talking around the fact that the returns have been lower by only a few percentage points or even less than one per cent. But as we know, even less than a per cent can make a material difference.

Twenty-five per cent of those surveyed did not understand the danger of predicting the future on short-term past. That is another concern of people being susceptible to misleading behaviour. The single most worrying thing in this environment was that 32 per cent of the people surveyed thought that a bank account was a suitable investment for retirement. One of the worst risks but one of the most invisible risks is that people worry about negative returns but they do not worry about the potential for not earning enough to exceed inflation. That is one issue in particular. If 32 per cent think that a bank account is a suitable investment for retirement then we have some major work to do out there.

Only 39 per cent surveyed correctly picked the growth assets in a particular survey, which were shares. ANZ conceded that that may have been because the stock market was performing particularly badly, but that in turn, I think, reflects the fact that people do not understand that earlier point. A lot do not understand that good assets have short-term fluctuations. Even though the stock market had been performing badly at the time the survey was conducted, that does not mean that they are not growth assets; they are still growth assets for the long term. If only 39 per cent picked shares as growth assets that is also a concern. Also, 19 per cent could not name a single disadvantage of having a managed investment. So 19 per cent did not realise that managed investments could decline in value.

Those highlights from the ANZ financial survey show, we submit, that a lot of work needs to be done out there before we have unfettered rein on choice of funds. I guess that segues into the ASIC-ACA shadow shopping report on financial advisers. Without spending too much time on

that, it is a concern that 51 per cent of the plans were borderline or below and 80 per cent were okay or below. We are talking about fewer than 20 per cent of the financial plans being adequate by any reasonable measure.

As a final point—and perhaps this is another example of lack of financial literacy—48 per cent of the people surveyed who preferred commission based advice as opposed to upfront fees thought it would motivate the adviser to give better advice. They obviously drew some kind of correlation between the commission being in proportion to the return on the investment—that is, if a planner advises you to go into a better investment, they would get a higher commission—rather than being aware that the commission was based on the initial placement and ongoing capital inflows and that it really did not matter how well or how badly that investment performed in future. Unless it was so extremely badly performed that you pulled out of it, they would continue to get their commission irrespective. There is a lot of misunderstanding out there. That is our major concern. We would like to see the government in conjunction with the industry—because we certainly have a role to play—finance and resource considerable education and information campaigns prior to an introduction of both choice of funds and portability in a synchronised fashion, because the issues facing both are the same.

**CHAIR**—The issue that you raised in relation to financial planners is a matter which the committee have been very involved with. We had quite a lot of discussions on this with the Financial Planners Association when we met. Many of their top people are now providing upfront transparent fees and charges. This seems to be a trend, which is encouraging. At the same time, I think they are doing a lot to upgrade the qualifications of people who are operating under their umbrella—which is certainly a move in the right direction. The previous witness outlined a plan where he believed portability would be acceptable in that inactive accounts could be transferred to an active account. Would you object to that?

**Ms Galbraith**—This is done automatically?

**CHAIR**—Providing the protocols were satisfied.

**Ms Galbraith**—Once the account is inactive, we have no issues with portability and accounts being transferred. It is really only an issue for us when they are still active. It is a bit silly to have incoming and outflowing into the same thing. So, no, we would support that. By and large, the industry sector funds and the corporate sector funds—and I am not so sure about the public sector funds—tend to have portability of inactive accounts. There tend to be conditions with ceasing employment and occasionally with leaving the industry, because there are industry funds where people might cease employment all the time but still work within the same industry. But for most funds the conditions are to do with ceasing employment, and once a certain period has passed they currently allow portability—it is a current phenomenon—with, as Mr Silk pointed out, relatively low and generally cost recovery exist fees.

**CHAIR**—So that is a possibility that may offer some progress in the portability debate?

**Ms Galbraith**—Our preferred option is in conjunction with the choice of funds. If that is not to be the case, our second preferred option is that it is permissible; that once the incoming contribution flow has ceased and the account is inactive it is subject to portability but that while it is still receiving contributions it should not be.

**Senator BUCKLAND**—I have a hypothetical question that I want to put to you, but I want to make the comment that the education of people in super schemes is something that is increasingly worrying to us. Over the last couple of days we have talked about some way in which we might be able to address that. This is not the hypothetical question, but do you think the funds in general would be supportive and cooperative in looking at a way to educate members of super funds?

**Ms Galbraith**—Yes, definitely the industry funds and, I would suspect, a lot of the corporate funds—the very reason corporate funds exist is to try to do the right thing by their employees—and, I imagine, a lot of the public sector funds as well. I cannot really speak for the retail funds, and that will vary considerably. But certainly a lot of the funds that I have been involved with, both corporate and industry funds, go a fair way down that track already with their information material and their disclosure material and also in running seminars. I think corporate schemes, in particular, are especially good at running seminars, and certainly a number of industry funds do so as well. Some of those are focused more on pre-retirees, but others do run seminars at various workplaces. The industry is probably the most logical delivery mechanism of that education and training, in conjunction with some of the regulatory bodies and the government. It really needs to be a combined effort.

I noted—and I think it might have been in your report; I have been doing a bit of reading recently; it might have been in a submission to your previous inquiry—that efforts are being made to introduce it into the curriculum at schools. In the medium term, that is ideal. It really does need to be part of education per se. That will help on a rolling out basis, but, for the members and employees out in the work force at the moment, I guess the other bodies to look at are the employer associations. It would be helpful to get them on board as well and have them involved as part of the employment environment. Perhaps employers should speak to their employees as much as funds speak to members, even though we are talking about the same individuals, and approach it together or even in different directions.

It is in everybody's best interests for members to receive education. I was going to use the word 'information', but the word is 'education', because I think sometimes there is a danger of information overload. While I am all for clear, concise and effective disclosure, which is what FSR advocates, there is still a propensity sometimes to over disclose. But, even more importantly, even if the information is clear, concise and effective, people still need to have the ability to process that information. That is where we really need to help with more fundamental education.

The ANZ survey and the shadow shopping survey are interesting, because it is broader than just super; it is general financial awareness and, in some cases, numeracy. That is another area where it is not just super funds with their members but also other investment bodies whose investors, in whatever form it takes, might get together for general education. It is really more about investment than it is about super. For example, when you are making a choice of funds, you are pretty much comparing apples with apples unless you are doing something like defined benefit to defined contribution. You are pretty much making an apples with apples comparison once you have done some basic education about different fee structures, and that is probably the major difference, and different returns. I guess we need to education people more fundamentally about those kinds of things—what differences in returns make and what differences in fees and charges make when they are choosing between super funds or other investment vehicles.

**Senator BUCKLAND**—If you look at the ANZ report—and I do not pretend to be able to analyse those figures very well—on first reading it gives you the thought that it is the script for a comedian at an accountants club or something. It is really frightening when you look at it. The whole education thing is something that we are beginning to get a responsibility for looking at. It is all right to say, ‘We’ll make it part of the curriculum at schools—there’s no better way to do it.’ But what do you do for the people already in the system? They are not at school. That is where I think we need to have a broad look at that. That is an observation more than anything. I was interested in your comments.

**Ms Galbraith**—With disclosure, we need more effort going into formulating relatively standardised disclosure across the industry so that it as standardised as possible so that it facilitates apples-with-apples comparison—or, if it is apples with oranges, people are aware that it is apples and oranges—and it has consistent, almost prescriptive, mandatory terminology that will aid people to come to terms with what particular definitions and expressions mean rather than having two different competing products calling the same things different names and so people think they are different things or calling different things the same names and so people think they are the same thing. I think there is a probably a role to be played there. From the regulator perspective, ASIC is probably the key regulator. It has already done a lot of good work on disclosure, but that certainly needs to continue.

**Senator BUCKLAND**—The final thing—and this is my hypothetical—that I will ask you, because it has been a very good submission, is: if Superpartners had a choice to leave the system untouched or to introduce these regulations, with or without choice attached, which do you think Superpartners would choose? I know that is a hard question and you might need to consult people, but I would interested in that.

**Ms Galbraith**—It is little bit difficult to answer because we are here on behalf of the funds that we administer, some of whom are members of the Industry Funds Forum, but I would be inclined to say that it would be the system as it currently is, simply because our funds generally, as Senator Watson alluded to earlier, once the account is inactive, do allow portability anyway. So we would prefer the status quo rather than the regulations as gazetted yesterday.

**CHAIR**—Thank you very much, Ms Galbraith.

**Proceedings suspended from 10.22 a.m. to 10.39 a.m.**

**HEWETT, Ms Helen, Fund Secretary, Cbus**

**NOBLE, Mr Gordon Andrew, Employer Coordinator, Cbus**

**CHAIR**—Welcome. I invite you to make an opening statement and we will have some questions following that.

**Ms Hewett**—Thank you for this opportunity to make a verbal submission to the Senate committee's inquiry. You would have heard us on many occasions giving you an outline of Cbus and the fund. I do not believe we need to do that today. What I do want to remind people of is that when Cbus was formed, one of the aims—and indeed the basis for industry funds—was to facilitate portability, because we have now almost 34,000 employers participating in our fund and very often work in the industries we cover is project based and for fairly short periods of time. So portability is very important, and we see it as critical in allowing members to accumulate superannuation balances.

In the draft regulations, the concept of portability has been taken to the next step, allowing members to transfer part of their balances. The logic of portability is that an individual should have the right to control their own super fund, given that they are reliant on those funds in retirement. Whilst the government has mandated nine per cent of gross earnings to be paid into super, clearly an individual's retirement income is based on more than contributions alone. The additional contributions of members are very important. We see investment returns, fees and charges as a critical part of this accumulation of benefits.

In the current superannuation system there are basically two types of funds. There are those that are for the benefit of members only and those that exist to make profit for members, for their shareholders. I do not believe that there has been evidence to show that the for-profit funds, if you like, have outperformed the not-for-profit funds. In fact, in the last year or so, I think the evidence might be to the contrary: the not-for-profit funds have outperformed.

We have seen during this period of low investment returns—and previous to that when we had negative returns—that members have very much been focused on fees and charges. In fact, some work that we have done talking to members on sites has shown us that a lot of members that have active contributions coming into their accounts are totally unaware of the crediting rate. Even though it is well-publicised, they are very much unaware of that rate. They really are looking at the bottom line. The members that have reacted most strongly in periods of negative and low returns have been those with inactive accounts, who have been very focused on the fee. Because they are not receiving contributions, their account balance is actually decreasing rather than increasing.

As a result of this, we have experienced over the last 18 months very significant amounts of rollovers coming into Cbus from members who have been seeking to consolidate their superannuation to try and save on these fees and charges that have been highlighted. There have, however, been many obstacles for these members. Those obstacles have very often been around what we believe to be excessive exit fees that are being charged to pay for commissions that have been paid to agents, on many occasions probably some years before. Also there have been

charges associated with financial planners and advisers, and servicing shareholders with dividends. This is one of the main differences between the for-profit funds that pay dividends to shareholders and the not-for-profit funds: the question of fees and charges and the level of those. There seems to be no limitation in the portability regulations on the entry, exit, investment or administration fees. We think this really is an important issue that needs to be dealt with.

We understand that there are about 15,000 financial advisers in Australia and most of those are remunerated with some configuration that includes a commission base. Up until now, a lot of these financial planners have been able to charge fees. Very often, our experience has been that people do not understand what those fees are or the quantum of the fees. As I said before, this has become much more evident to people in a low-return environment. We think that financial planners can play a very constructive and very positive role if there is no conflict of interest, but our experience, again, has shown that very often there is a conflict of interest between getting a good retirement outcome for the member and making sure that the financial planner's remuneration is maintained. We see this as a problem in a commission based environment, and we think that commissions should not apply to mandatory contributions.

**CHAIR**—Which commissions? Trail commissions?

**Ms Hewett**—Commissions, but in particular we think trail commissions are amongst the most problematic. The question is: will the financial planners recommend what is in the interest of their client or what is in their interest? We know that there are a lot of financial planners who, when we make these statements, get very offended and say, 'This is not the case.' But we have to say that, with 360,000 members and vast numbers of rollovers in the last 18 months, we have seen enough evidence to show that this is a real issue, that members do not understand the level of the commission and that these commissions are excessive. I think you have seen evidence of this, and we have tendered some information in our written submission to show the level of some of these commissions that are being charged.

Cbus want to make a number of recommendations and have done so in our submission. Those are basically: that commissions should be banned from transferring superannuation balances, that there should not be a commission associated with that transfer cost; that there should be a cap on exit fees; and that the exit fee should reflect the cost of processing the benefit payment to enable someone to consolidate their superannuation. We do not think other members should have to subsidise this cost, but we think the cost should not be excessive. In our fund we charge \$35 and that covers the total cost, so there is no cross-subsidy, but clearly some smaller funds may have to charge a bit more than that. We think thousands of dollars, and what is in some cases all the benefit, is well and truly excessive. We also think the transfer protocol that a number of industry funds have tried to work with needs to be considered. That really needs to be right across the industry so there is real cooperation between service providers and superannuation funds, so benefits are transferred efficiently and members can consolidate their funds.

Another very important issue that needs to be looked at by this inquiry is group life cover. We have on a number of occasions highlighted to the Senate select committee the problems we see with group life cover. Clearly, in an industry such as ours, it is very important to our members—and our surveys of members show that it is amongst the most important of the benefits the fund provides. They work in a high-risk industry where there are many injuries and the jobs, as we say, are very often project based. Most of them would find it very difficult to get insurance on an

individual basis, because there are many pre-existing conditions. Even complaints such as asthma will very often rule out people who need to submit themselves to medical examination before they can access insurance.

In a fund such as Cbus, where we have an automatic acceptance level, anyone who is starting work with a new employer and joining Cbus can get insurance of up to four units of cover, which is a quite significant amount of cover, regardless of any pre-existing conditions. So, as long as they are at work—and, of course, their contributions are paid so the premiums can be paid—they can get this insurance cover. We see this as a real problem that needs to be addressed, because we think it is a significant part of the compulsory superannuation scheme that a lot of workers have access to death and disability cover. My colleague Gordon Noble is now going to highlight a couple of the issues I have just raised in my summary, if that is okay.

**Mr Noble**—I want to start with the issue of insurance, which we have just been talking about, and flesh out some of the issues in a little more detail as to why the introduction of the portability regime, as it would stand, would threaten the ability of a fund, such as Cbus, to offer a group life scheme. The basis of the insurance that we offer to our membership is that we have a pure risk pool—that is, if a member of Cbus automatically has the entitlement to the life insurance. What would happen with the arrangements with portability is that you may have people who are transferring out of Cbus and maintaining another superannuation arrangement, which would mean that they would potentially have other life insurance arrangements. When we come to negotiate our arrangements in terms of life insurance and total and permanent disability, we do so with a life insurer. That life insurer, in a new environment, will be asking us a few questions. They will be saying, ‘How can you guarantee to us that the people who are transferring out of the fund, as a result of this regime, have not got alternative life insurance arrangements and that they are not moving for those life insurance arrangements? How can you guarantee to us that the pool of risk that we are effectively covering has not been effectively changed as a result of these arrangements?’ I think we would struggle to answer that.

The result of these regulations would be that the insurer would say to us, ‘The risk pool that you have has now changed. We are concerned that we know that some of the best risks—people who could get the best rates of life insurance—have left the fund, have established other arrangements and left in the fund are people who perhaps have the higher risks.’ The options for the insurer would be to say, ‘We now need to either reduce the benefits or introduce underwriting.’ At the moment, Cbus does not underwrite individuals in terms of that access to up to four units of insurance. If we were to underwrite every individual for insurance purposes who came in, not only would we find that some would not be accepted for insurance but the costs of underwriting those people would increase the costs ultimately of the insurance benefit. The underwriting cost would, in the end, be reflected in the premium and the benefits payable to members. We are arguing that the portability regime would have a significant impact on the ability of funds such as ourselves to continue to offer what is a significant benefit in an industry which is based around dangerous practices at work and dangerous occupations.

I want to turn to the issues of consolidating accounts and flesh those out. We are arguing for a transfer protocol, as we have just discussed. We believe that, in terms of the practices in the industry and consolidating superannuation accounts, good practice is not exercised by all participants in the industry. We believe that we operate on a basis of professionalism, trying to process rollovers as smoothly and professionally as possible, but we do believe that there are

some providers out there who will delay the processing of rollover requests and who ultimately ask for their own forms to be used. When this is done, it creates another obstacle for members because members find it difficult enough to understand the superannuation system without being pushed through another hoop in terms of consolidating their superannuation accounts. We believe that we need some transfer protocols to ensure that we do get a consistency of standards across the industry in terms of rollovers.

The second thing we would like to talk about briefly is the issue of preservation funds. You may be aware that we use our own preservation fund—the Australian Preservation Fund. This fund actively tries to find homes for people who have had superannuation transferred to it. We do not believe that that is the case in other preservation funds that exist in for-profit superannuation providers. We believe that this is an issue that the committee should turn some attention to if the federal government is genuinely interested in consolidating the number of superannuation accounts across the country.

Finally, I will talk briefly about fees and charges. We believe this is a significant issue. We believe the entry fee represents a significant cost. We know that in practice, while there are many financial planners who have the highest standards and levels of integrity, there will be some who will be attracted by the fact that they will be able to target people with significant account balances who potentially they could not have talked to previously about their superannuation arrangements. They will talk to them about transferring superannuation into other arrangements.

I reiterate that, whilst there are high levels of integrity on the part of many financial planners, the reality is that there is still an incentive for financial advisers to put an individual into a product in order to earn the commission that will come from that. The higher the balance, obviously, the higher the commission an individual can earn. In a number of funds they have not had that ability to transfer these superannuation balances into different products. With 15,000 planners out there, the reality is they will be talking to many consumers out there, and many consumers will not potentially realise what it is that they are signing up to. Even though we have had improvements in terms of the Financial Services Reform Act, which provides for disclosure, the reality from talking to our members is that there is still a great deal of confusion about financial services products and superannuation in particular.

We have seen the mis-selling of pensions in the UK. That resulted in \$11.8 billion in compensation being paid to consumers as a result of the practices of financial planners in that country. We do not want to see a situation like that in this country. We believe the way to avoid that is to ensure that, if we do introduce a regime such as the one we are discussing today, it is introduced with appropriate safeguards. By that, we mean there is a need to ban commissions to prevent these practices. We do not believe commissions should be earned on what are mandatory superannuation contributions.

**CHAIR**—From a legal point of view, employers have a responsibility to transfer nine per cent into a superannuation account. I wonder—and I not sure whether this has ever been tested—about the legal implications of an employer putting a person into a scheme where a person is denied the benefits of anything less than nine per cent after deducting government taxes. Have you looked at that?

**Mr Noble**—From our point of view, we believe that the standards we operate, in terms of the industry funds and Cbus in particular, are the highest standards because we are here not to make profits out of members but to provide the benefits. If a framework were to be introduced which looked at all these issues—investment fees, administration fees, entry fees and exit fees—we believe that we would be operating a standard that would be of the highest nature in any case. But there is an issue. Not all employers pay superannuation contributions to funds such as ours. Many pay them into for-profit funds. Many members, therefore, have administration fees and other fees and charges which are higher than we believe they should have. We would like to have everybody in an industry fund and for everyone to have that opportunity. We do believe that there is an obligation to ensure that superannuation guarantee contributions, in particular, are not diverted for other purposes.

**CHAIR**—I was not referring so much to the ongoing administrative fees, because depending on the complexity of the product some funds may have higher administrative fees than others, and I acknowledge that. If it is transparent, people are paying for what they get. What does worry me is a situation where, in relation to the obligation to pay the nine per cent, through an exit fee that amount, technically, has the ability to be severely diminished. It appears that because it is a contract nothing can be done about it, unless you introduce retrospective legislation. Have you looked at that?

**Ms Hewett**—No, I do not believe we have. But we have looked at rollovers out of the fund and where they are going. A lot of rollovers are going into do-it-yourself superannuation funds. Our inquiries show that in almost all cases there is a third-party adviser involved who is advising the person to put the money into that do-it-yourself fund. In a lot of cases, although we have read statements from financial advisers saying that, generally speaking, a do-it-yourself fund is not applicable or beneficial to someone who has less than \$50,000—

**CHAIR**—It is higher than that.

**Ms Hewett**—we are seeing amounts of \$5,000, \$17,000 and \$30,000 going into do-it-yourself superannuation funds. Then members come back to us after the event and say, ‘I’ve been stung. What do I do? I’m now in this fund, but I don’t really know how to manage it,’ and so forth. There is a very big issue there, particularly in some industries where people move from being employer sponsored to being self-employed and where there is a lot of project based work. This is not just an issue for the construction and building industry, because there is a lot of casualisation, project work and so forth in other industries as well.

**CHAIR**—We are told that under the new FSR rules financial planners who give such advice will be in trouble.

**Ms Hewett**—But how do they get into trouble? There has to be process that is followed where someone lodges a complaint and so forth. Very often, in our experience, people see that as being in the past and that they are not going to win against these institutions, these big organisations which are sometimes franchised and so forth. Even when there is an excessive exit fee of, say, 80 per cent being charged and we say, ‘We’ll try to pursue it for you with that financial institution and argue that it’s unreasonable,’ sometimes the member will say, ‘No, I don’t want to cause a fuss. I have insurance’—or a business loan—‘through the financial institution. I just don’t want to rock the boat. I will leave it be.’

**CHAIR**—You now have a very proactive regulator in the form of ASIC that is quite anxious to take these issues up under the new reform legislation powers. So, hopefully, in future we will see a lot less of that, particularly if there is exposure given to a prominent case.

**Senator CHERRY**—I want to follow up on a question I have asked a couple of witnesses and that is the notion of how we get to a transfer protocol. You spoke about the importance of that and I have heard more about the transfer protocol in the last two days than I have heard in half-a-dozen years. What are the steps that we need to take from here to get people to sign up? A related question is: what are the categories or classes of superannuation fund managers who are causing difficulties in terms of the transfers that you were speaking about?

**Ms Hewett**—With the transfer protocol, we would like to see a standard rollover form that was simple. Very often people know that they have money with somebody and are not sure exactly which product—some financial institutions operate with many different products—because they have lost the piece of paper that has their member number on it and so forth. For those people, there is very often little cooperation in helping them. Whereas when someone wants to roll money out of our fund, we will fill in part of the form—writing their member number and the details that we have on record—to assist them, particularly people who have literacy and language barriers.

There needs to be a simple and uniform standard form that is introduced and there needs to be a level of cooperation. Very often the fund member will become annoyed with the receiving fund because they have made the request for the rollover to the receiving organisation—say, in our case Cbus—and there is a very long delay. Yet we have very little power to demand of the transferring fund that they expedite the process. There have to be better rules that people have to abide by about transferring money. Clearly, in some cases, there has been a lot of delay and it is improved by quarterly SG contributions, but it is not financially efficient for a fund to transfer a benefit and then a month later receive another contribution and then have to transfer and process another payment. It is not good for the member and it is not good for the funds. Sometimes you have to wait until you receive the final payment that is due, if you are leaving an employer, from that employer.

So there are issues to look at in the administration of it. An organisation cannot always transfer the money immediately but we have had members in some cases who have filled out the forms numerous times and the organisation has lost them several times—they say that they have never received them—and the member basically gives up. There needs to be some level of cooperation and maybe some penalties if people do not comply. There needs to be a standard form in the first place. The form has to be very simple. That is one of the steps that could be taken.

**Senator CHERRY**—On page 5 of your submission you talk about the consolidation of accounts and you suggest that there are other means of promoting consolidation of accounts than this regulation. Very briefly, what principal reforms do you think we need in that area?

**Ms Hewett**—We think the principal reforms are around the question of fees, so that people can make a decision about what is best for them and not have huge penalties associated with making that decision. We see that as the biggest barrier and the process itself and the level of cooperation as other barriers.

**Mr Noble**—Adding to that, I think it would be beneficial to have an obligation on the preservation funds to try to find homes for the funds that they have there.

**CHAIR**—Can you explain your concept for the ideal preservation fund?

**Mr Noble**—We can talk about what our preservation fund—the APF—does, which is to actively try to match funds. Where we have information that a person has a superannuation fund, we try to identify a process to match that person's new superannuation fund and transfer the funds in the APF to that fund. The idea that the APF sits and simply goes on over the years, accumulating different amounts of money and never trying to find a home for them does not seem to be a sensible notion.

**Ms Hewett**—I think the success of it was highlighted in a recent pilot that was conducted, where a number of industry funds, including the APF, together with the Australian Taxation Office and CMSF, had a week of trying to find lost superannuation. Millions of dollars were located, and that was just a small pilot with a lot of voluntary labour trying to facilitate this. Also, when people join the Australian Preservation Fund they sign a form authorising us to search for lost super. I think that it is very important that funds try and help members, because they are not aware of all these other places where super goes, such as the ATO registers. They are not aware of preservation funds. Even though they are told in their forms and so forth, they are really not aware or conscious of it.

**Senator CHERRY**—How much progress do you have with it after people sign those forms? Do you find a lot of accounts?

**Ms Hewett**—Yes. Every quarter we have transfers of inactive small amounts coming back into the fund because the members become active again in the building industry. It is very important in our industry—but I think you would find there would be similarities in others—where you are inactive for a period of time because there is just no work in the particular state or territory that you are in, so you go off and work in another industry. Then you will get work in the industry and we will start receiving contributions, so we will search the APF to see if there is money, provided you signed and authorised us to do that. If there is money there it will be consolidated, at no cost to the member.

**Senator CHERRY**—Do other preservation funds have that arrangement with you?

**Ms Hewett**—No. Each fund nominates one preservation fund to help members try and locate their money so there is no confusion. I do not believe that this is commonly done with other preservation funds. We are suggesting that the issue of full-profit preservation funds probably needs to be looked at.

**CHAIR**—Thank you very much for appearing and for the information you have given to the committee today. We appreciate it.

[11.14 a.m.]

**WARD, Mr John David, Manager Research and Information, Mercer Human Resource Consulting Pty Ltd**

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

**Mr Ward**—Our firm manages, on behalf of its large corporate clients, quite a large number of corporate superannuation funds. We also operate our own master trust, which is one of the largest in Australia. This morning I want to talk about several issues, in particular the linkage to choice of fund, the problems with effective disclosure and mis-selling, the costs of the portability proposals and also the surcharge implications. Mercer are not opposed to either choice or portability. However, we believe that before they are introduced there needs to be some major changes. In particular we are concerned about effective disclosure and the need for an education program. That applies to portability just as it does to choice of fund. We think it is totally illogical to introduce portability without choice. It seems crazy that a member can transfer his benefits in his current fund if the next day there are going to be further contributions going into that fund. I would agree with Mr Silk's comments earlier that this is likely to increase the number of member accounts rather than reduce it. In the system there are a lot of inactive accounts. Our view is that most of them are there because of member apathy rather than any other reason.

In the hundreds of funds we administer, I am not aware of any that charge excessive exit fees. They might charge a benefit processing fee. In some cases the costs of selling the assets might be passed on to the member and in some cases the plan design might appear as though it is an exit fee whereas in practice it is not. I am talking there about funds often set up many years ago where the employer agreed to provide a higher level of benefit to those who were prepared to leave their money in the fund until retirement, so there was an encouragement to save for retirement. If you took your money out early, you got a lower benefit; if you left it in there to save for retirement, you got a higher benefit. That might have been achieved through vesting scales or in many defined benefit funds the promised retirement benefit might have been higher than the resignation benefit, and you could have availed yourself of the retirement benefit by leaving your money in the fund. In such cases that would not mean there would be a reduction in the SG or the mandated portion of benefit. It is really that the employer has made additional voluntary contributions that might have been only payable if the money was left in until retirement. A lot of those funds have changed over the years and the preservation rules have made a lot of that sort of arrangement redundant.

One of our major concerns is mis-selling. We are not comfortable at the present time that the financial planning industry has its act together and that members will not be mis-sold inappropriate superannuation funds. FSR comes into play next year. We do not know how it is really going to operate and how effective it is going to be, but certainly under the current FSR rules we do not believe the requirements for effective disclosure are strong enough. They need to be strengthened. We have seen the problems that have occurred in the UK and other overseas countries where some level of choice has been given. We do not want that to occur here.

I note that the new regulations that were gazetted this week impose extra obligations on the trustee of the member's current fund to provide additional information. We have not had long to analyse those—and I have not had a chance to discuss it with my colleagues—but I find it very unclear what those requirements impose on trustees. I think those rules would certainly need to be clarified. But again there is nothing there that provides additional and appropriate disclosure by the new fund. With regard to costs, portability will increase the costs of superannuation funds. There will be more benefit payments to process, and they all have a cost. Somebody has to pay, whether it is the member who is asking for his benefit to be transferred or whether the cost is shared amongst all of the members.

Yet looking at the changes that were introduced in the gazetted regulations, there are a couple of changes that will help in that regard. Firstly, there is the 12-month rule, and that is one of the suggestions we had earlier made to Treasury. I am pleased to see that there is such a provision so that trustees do not have to make multiple transfers for a particular individual. However, I do have a concern with the way it is written in that, whilst it is appropriate for funds where there are likely to be continuing contributions, if the benefit is in an inactive account and there are no future contributions, I would not want to see trustees using that 12-month rule to stop a member from, say, transferring half of his benefit to a particular rollover fund one week and then refusing to transfer the other half the following week. Again, I have not had a chance to discuss that with my colleagues, but perhaps restricting that rule to situations where there are likely to be further contributions might be a safeguard.

Secondly, there is the other new rule regarding the \$5,000 minimum balance. I am not sure why that has been introduced. One suggestion is that the \$5,000 minimum has been introduced because of family law issues and splittable payments. That may well be the case. In our earlier submissions to Treasury, we were concerned about members transferring all of their existing benefit in a fund if they were continuing members, because the following week there might be a need to deduct an insurance premium from their account. If there is nothing left in the account, that could result in the insurance cover lapsing. If the employer had put in more money in the meantime, maybe that would have been enough to cover the insurance premium, but if the employer does not put in money for another two months or so, another eight weeks of insurance premiums could have gone by—insurance cover is gone. So all of a sudden the member has lost his death cover unexpectedly.

We thought that maybe this \$5,000 was an attempt to offset that problem, which I am sure it does. So it is a big help there. At least with \$5,000 there, in many cases that should be ample to maintain the insurance cover until the next employer contribution comes in. However, again I am concerned with the wording of that particular provision because it still seems to enable the member to transfer the whole of his benefit. I am not quite sure what that means where we have still got an active account. If he transfers all of his benefit and we have still got to provide insurance cover, that loss of cover problem still exists. My view is that that provision should be changed so that for any active account the trustee can maintain at least \$5,000 to provide that continuing insurance. Even that is not foolproof because we have got something called surcharge; and, out of the blue, the fund might receive a surcharge assessment for the member which will wipe out that remaining \$5,000 or \$3,000—whatever is left—and again will run into problems with the insurance cover lapsing.

That particular provision is also written in a very strange way, and I do not understand what it means. I read the explanatory memorandum and I do not understand what that means either. It talks about the value of the member's interest of \$5,000. The value of the member's interest is not defined. We do not know whether you are supposed to take into account the value of the death benefit that might be continuing, whether it takes into account the value of any unvested benefit. For a member who has also got a defined benefit in the fund, does it take that into account? It is too unclear and needs to be defined much more specifically.

We have heard today some talk about limiting exit fees. As I indicated earlier, I was a little surprised to hear the extent of the high exit fees, raised by Mr Silk. Certainly we do not see those high exit fees in the funds that we are involved in managing. I am certainly not aware of any particularly high number of problems in that area for funds where we are getting moneys transferred from. But there are significant costs involved in processing a benefit at any time. There is the verification that the member is who he says he is. There is the determination of benefit. There is splitting the benefit into its various tax components. There is splitting the benefits into its various preservation components. There is the liaison with the employer to ensure that all of the contributions have been paid, because we certainly do not want to have to pay another small benefit two weeks later when we get the last contribution. We have to report to the tax office for RBL reporting. We have some surcharge reporting to do. We have to calculate the tax and pay it to the tax office. We have to report to the member. We have to issue a payment summary. We have to ensure we have the necessary details of the rollover fund, because if we do not have those we will not be able to pass on the surcharge assessment. We have to draw the cheque and, under these new provisions, the trustee would have to provide additional information and make sure the member does not want any further information before he can make the benefit payment or transfer. We find that the real cost of making a benefit payment is probably greater than \$100, so in any limitation of fees we really need to take into account the significant work involved in processing these payments.

**CHAIR**—You said it is in the order of \$100. I think the worry is where it is significant and runs into thousands of dollars.

**Mr Ward**—That is a concern. We wholeheartedly support efforts to stop fees at that sort of level. We just need to understand what the fees are. As I mentioned before, if the employer has decided that he wishes to provide additional voluntary contributions that might only be paid at some future point, the employer should be allowed to do that. It should not be considered a fee. If we are talking about significant fees on mandated or SG contributions, we would agree.

I would also like to say a few things about the 'S' word—surcharge. Surcharge is a concept that I would say is totally alien to the superannuation environment. The legislation uses words that have never been used in a superannuation context before. It is like hammering a round peg into a square hole. There are cracks all through the peg. There are gaps down the sides and it has really only worked to the extent that it has because of a huge amount of effort put in by the tax office and a huge amount of effort put in by funds and their advisers to try to come up with a system that barely copes with the requirements. It is staggering along. When portability is introduced, the problems are magnified considerably. The biggest problem is who pays the surcharge. It is actually the obligation of the fund that holds the contributions that is liable to pay the eventual surcharge assessment. From a practical point of view, even though I have trouble

understanding the concept of holding the contributions, if there has never been any benefit transferred out of the fund it is pretty obvious that that fund is the holder of the contributions.

If, when a member leaves the employer, the whole benefit is transferred to another superannuation fund then it is fairly obvious that the new fund has become the holder of the contributions. But if we are transferring half of the member's benefit, which fund is the holder of the contributions that related to the surcharge assessment? Did the fund pay out the contributions it received 10 years ago or is it paying out the contributions it received this year or last year? There is no tying the legislation requirements for surcharge to what is actually being paid out here. How you would actually do that legislatively I have got no idea, it is just too complex. But we need some sort of protocol established so that funds know here at least is a standard that we can all follow that asks, 'If you've transferred half your benefit, is that the first half of the contributions or the second half? Which year's contribution is it?' There is a lot of work involved in establishing that protocol. It is not going to be easy, but it needs to be done if surcharge is going to work at all. If it is not done we are going to have arguments between funds and we are going to have arguments between funds and the tax office.

Systems need to be changed to cope with surcharge. The way most funds operate at the moment is: if the member has still got some money in the fund when the fund receives a surcharge assessment, the fund will pay that surcharge assessment. The whole system has been designed around that. That might not be what the member wants; the member might want the surcharge paid from his new fund. But let us say the member has got \$5,000 left in his account and the fund gets a surcharge assessment for \$6,000. Because the system still recognises that the member is an active member, the current system would actually pay the full surcharge of \$6,000 to the tax office. But the member has only got \$5,000 in his account—the other \$1,000 has come from the fund as a whole. Other members are going to effectively have to wear that cost or alternatively the administrator is going to have to go down and carefully check every surcharge assessment—hundreds of thousands of them—every time the assessments are issued because the system will not do it automatically. It would have to be manual to make sure that, 'Yes, we did have enough money in the funds to pay the assessment,' or, 'No, we've only got \$5,000 left in his account; we'll pay \$5,000 and we'll have to send the other \$1,000 assessment back to the tax office.' It is going to be a mess.

We have already got problems where we have got to report manually to the tax office. Where we roll over a benefit to any fund, the tax office requires us to get the ABN of the rollover fund. There are many tens of thousands of self-managed funds that do not have an ABN. If we get a surcharge assessment for a member where we have rolled him over to a fund that does not have an ABN, we cannot process that electronically. The tax office will not allow it. We have to process it manually. If we bring in portability there are going to be a lot more transfers to self-managed funds, many of whom will again not have an ABN, and we have got some real reporting problems there. In our view, those problems need to be sorted out before portability is introduced and there are going to be some very significant changes to computer systems needed to implement whatever protocols or changes are made. At least 12 months should be given after those protocols are determined before portability is introduced.

To summarise Mercer's views, we would consider that portability should be introduced at the same time or later than choice of fund, certainly not before. We believe that the government needs to address issues on member education, disclosure and the quality of advice, to minimise

the risks of mis-selling. We believe that funds need more time to implement the necessary changes that will flow on from portability—as I said, at least 12 months after any changes to surcharge legislation or protocols are introduced. We need to provide a means of ensuring that members' cover does not lapse unintentionally. I would also pick up one of the points made by the previous speaker about concerns about loss of automatic acceptance cover through the introduction of choice/portability. We need to address problems with surcharge reporting and assessments before portability is introduced and, really, 1 July 2004 is too early.

**CHAIR**—Thank you very much, Mr Ward. I think the committee members can appreciate why we keep calling Mercer for information and submissions. It is always high quality and very good. We do have a problem in terms of casuals and their insurance, as you referred to. If we change the rules to make sure that an inactive account is one to which no contribution has been made in the last 12 months, particularly if we had a restricted portability—for example, enabling people to roll over from an inactive account to the employee's active account, because a casual could have a number of employers on, say, a seasonal basis—would that help?

**Mr Ward**—I have no problem with requiring portability for inactive accounts.

**CHAIR**—Yes, but the problem is, what is an inactive account?

**Mr Ward**—I think all of our clients already do that: many of them encourage members to take their benefits once they become inactive.

**CHAIR**—But we can foresee a situation of 'What is an inactive account?' in terms of some casuals.

**Mr Ward**—It is obvious from the point of view of a permanent or part-time employee; casuals are more difficult. One way of doing it may be to put that 12-month provision in, as you suggested. There might be other cases where—

**CHAIR**—Would 12 months be too long?

**Mr Ward**—it is quite clear that perhaps the casual is not going to receive any further contributions. He might have gone and got a full-time job. In other cases—fruit-picking might be an example, where there is a yearly cycle of casual work—a 12-month provision would certainly assist. I do not think it would want to be any longer than 12 months; 12 months might be about the right time to pick up that cyclical type of casual work.

**Senator BUCKLAND**—I have no questions on your written submission. Of those funds that you deal with and you are consulting to, and the organisations associated with those funds, are you aware of any that would have exiting fees above 20 per cent?

**Mr Ward**—No.

**Senator BUCKLAND**—That strikes me as being somewhat different from other evidence that we have which shows a large proportion, about 61 per cent, are charging above 20 per cent. So that really does strike me as something different.

**Mr Ward**—Many of the funds that we are involved with would charge of fee in the order of \$100 as a processing fee. In some cases there might be the costs of actually realising the sale of the assets. That would be nothing like 20 per cent—it might be one or two per cent. Again, that would be fairly rare. You have to realise that the funds that we deal with are funds that have been established, in the main, by large corporations for their employees, either as a stand-alone corporate fund or as a subplan in our master trust. So in each case there is a significant employer involved. These high-exit-fee cases are more likely to be in a retail fund where the individual employee has been sold the superannuation plan rather than the employer choosing the plan for all of its employees.

**Senator BUCKLAND**—Does the fee vary with the size of the member's available funds? Would the exit fee for \$150,000 be different from someone exiting with \$6,000 or \$7,000?

**Mr Ward**—Generally not, no. It would be the \$100 type processing fee which would apply irrespective of size. If there are selling costs in selling the assets, that might be one per cent of the benefit. So a \$150,000 benefit might incur a slightly higher fee than a \$5,000 benefit—it would be one per cent of whatever the amount is. But, again, that is fairly rare.

**Senator BUCKLAND**—Has Mercer been involved with corporations that have been through the process of downsizing employee numbers and offering packages?

**Mr Ward**—Regularly.

**Senator BUCKLAND**—On those occasions were you are aware of any of corporations that brought in financial planners to help those people taking packages plan for their financial future?

**Mr Ward**—We have our own financial planning arm that often gets involved in those sorts of arrangements.

**Senator BUCKLAND**—But you are aware that that happens?

**Mr Ward**—Yes.

**Senator BUCKLAND**—What is the arrangement in that case? Are employees required to take advice or are they entitled to ask for separate advice?

**Mr Ward**—In many of those cases, if you go through the particular route that the employer has suggested, the employer will actually pay the costs of the financial planning advice. It is normally not compulsory for the employee to choose that particular adviser. I have never seen any situation where the employee has been prohibited from using another adviser. It might be that the employer will not pay for the advice from somebody else because it has a special package price with a particular financial planning group.

**Senator BUCKLAND**—But it fulfils the requirements, if you take financial advice?

**Mr Ward**—There is no requirement for a member to take any financial advice. He would be crazy if he did not and, again, he can choose whoever he wants. It comes down to a matter of who is going to pay for the advice. Often, in a downsizing situation, the employer puts its hand

in its pocket and pays for the advisers to come along and run seminars or even face-to-face consultations with individuals.

**Senator BUCKLAND**—In the case where an employee has been made redundant, how many of the corporate funds that you deal with allow the superannuation funds to remain in place once employment is severed?

**Mr Ward**—Most funds would make arrangements for that member's benefit to be transferred out to another fund.

**Senator BUCKLAND**—So even though there would be an exit fee of \$100 or so, there would be entry fees into a new fund. That in many cases would be taken up with the provided financial advisers brought in by the—

**Mr Ward**—In many cases where it goes to the employee's new employer fund, there may be no entry fees. In other cases, there will be an entry fee.

**Senator BUCKLAND**—But if they are being made redundant, in the main they are going into unemployment, until they find employment, so it goes somewhere.

**Mr Ward**—What normally would happen would be that the employee is made redundant, the fund would contact the employee and advise him that because he is no longer an employee he cannot stay in the employer fund but he can nominate whatever fund he wants to join.

**Senator BUCKLAND**—But that there is a planner who will be available for consultation, chosen and paid for by the fund, to give advice.

**Mr Ward**—In some cases, yes.

**Senator BUCKLAND**—That financial planner will more than likely recommend a fund.

**Mr Ward**—That does not happen all the time. In many cases, if it is just a one-off redundancy, there might be no financial planner organised by the employer or the fund.

**Senator BUCKLAND**—Whatever happens in that circumstance, the employee being made redundant is going to be stung with fees somewhere that will grossly eat into their superannuation savings.

**Mr Ward**—Normally you would give the member 90 days to make some sort of decision. If there is no response within that 90-day period, the benefit would be transferred to an eligible rollover fund where there are no entry fees. That is always a possibility. However, over the last few years we have seen a very significant reduction in the number of corporate funds as employers increasingly frustrated at the amount of time, effort and dollars that need to be spent to keep a fund running. So while the number of funds has been decreasing, the proportion of funds that enable the member to stay in the fund after leaving the employer is increasing. We are certainly seeing many more cases where the fund will allow the member to remain. Certainly that is the trend.

**Senator BUCKLAND**—As part of your consultation services that are offered to corporates, how much is budgeted for educating corporate superannuation fund members as to what is involved in their superannuation? Until I joined this committee, I did not realise how much it was involved. I just thought you took the advice of the employer and that they were always decent people, and went that way.

**Mr Ward**—I would not even hazard a guess at the sorts of dollars that are spent on that, but the amount is ever increasing.

**Senator BUCKLAND**—Would it be one or two per cent of the value of the fund?

**Mr Ward**—I doubt it would be that high. What are we talking about in educating members? Education is included in the annual report.

**Senator BUCKLAND**—That is hardly education, is it? It is an annual report. I would not think that would I sit down each night and study an annual report that comes from anything that I am involved in and say that I am being educated. It is not telling me how it got to those figures; it just says that you have gone bad or you have gone well. Education is understanding; a lot of these things are—

**Mr Ward**—Annual reports do include advice and information to help you understand the whole system. There is also information on web sites. Many funds are setting up their own web sites these days. There is educational material on them. There are seminars—

**Senator BUCKLAND**—That is a fairly broad sort of interpretation of education, though, isn't it? Is it on the web site or is it in the annual report that should things go the same way next year you might have to pay additional fees or if you leave the fund during the next year this is what it is going to cost you? Education is a fairly broad thing, but—

**Mr Ward**—I would agree. How many people would actually look up the web site to try to get educated? How many people put their annual reports straight into the bin because they think they are not going to understand them?

**Senator BUCKLAND**—Maybe that is because of the way they are presented. I am being given the wind-up signal.

**Mr Ward**—Certainly we are spending a lot more time in face-to-face seminars and individual sessions with members. Certainly that is one aspect that funds are increasingly getting involved in.

**Senator CHERRY**—I have one very quick question, Mr Ward. I want to reiterate the chair's comments that yours is a very helpful submission. One of your recommendations is about insurance cover, suggesting that trustees be entitled to hold back up to six months insurance cover. Does the government's changes to its regulations to require \$5,000 to be left in the account fix that issue, from your point of view?

**Mr Ward**—I think it does. It does not help the person who has only got \$200 in their account, but then that account would have run out anyway. The \$5,000 should cover the insurance

premiums in almost all cases until the employer next puts in a contribution—the only provisos I would make are, firstly, if there is a surcharge assessment that the fund receives which wipes out that \$5,000, or however much is left, and, secondly, if in an active account the member is still allowed to take out the full current account balance. If the ability take out the full current account balance was restricted to inactive accounts that would get rid of that problem.

**CHAIR**—Thank you very much, particularly for your information on the surcharge, which was very valuable.

[11.58 a.m.]

**BROOKES, Mr Nic, Chief Executive, Corporate Super Association**

**GODDARD, Mrs Elizabeth Jane, Head of Research, Corporate Super Association**

**CHAIR**—Welcome. I invite you to make a short opening statement. I presume you have seen the latest amendments from the government in terms of the gazetted regulations on portability.

**Mr Brookes**—We have. Thank you for inviting us here today. As ever, it is a pleasure to be able to share some views with you. As you have seen from our position, it has been slightly overtaken by the amendments to regulations as posted. So I would like to keep my remarks at this stage fairly strategic. We will go to the details through conversation, if that is acceptable. There are two positions. Firstly, there is where we are coming from. Just to restate our position, it is a not-for-profit position where the mechanism of the large corporate, employer-sponsored funds is provided at no profit and through a mechanism which is of the highest corporate governance. That highest corporate governance structure is the trustee board, which is half appointed and half elected. It ensures that the members—the employees or consumers—receive the best return for the lowest cost. That has been borne out by empirical research. For instance, APRA, in their February report, support that position.

Portability, from our point of view, is seen through the eyes of zero financial interest. We are looking at this purely from the point of saying that if this concept and its application benefits Australians that is good. If it does not, we will make some comments to seek to improve the position. Strategically, we support free markets and any application of free markets that allows the consumers—Australians—to have a better provision in retirement. Our worry about the current position on portability is that there are a series of steps that we feel need to be taken and that the current regulations are premature.

**CHAIR**—Mrs Goddard, would you like to make some comments on the technical aspects of the regulations?

**Mrs Goddard**—Not at this stage.

**Senator CHERRY**—I am very interested in the issue of investment reserves referred to at page 7 of your submission. Are you talking about defined benefit funds or about general accumulation funds where investment reserves could disappear as a result of the portability regulation?

**Mrs Goddard**—This could happen in any accumulation fund, depending on how they cater for fluctuations in investment returns. Some funds do that. Some will simply credit the return in the current year but some will attempt to smooth the returns.

**Senator CHERRY**—On the advice that one of your funds has received on capital guarantee issues, you say you understand that in at least one major fund where a capital guarantee is provided the actuary has indicated:

... if the regulations are made as currently drafted, it will be necessary to approach APRA to have the fund's ability to roll over amounts suspended under draft regulation 6.37.

How big an issue do you think that will be in your sector?

**Mrs Goddard**—I think that it will be an issue. We have not circulated on this to all our funds to find out exactly how prevalent these arrangements are, so we would have to take that on notice.

**Senator CHERRY**—It is interesting, because no-one else has raised it that I am aware of. I would be interested in seeing how much further we need to take that. The other issues I think we have largely dealt with at various times. It is pretty clear where things stand.

**Mr Brookes**—If I may, I would now raise a point about the steps we think are missing. It is really to do with corporate governance and independence of advice. I am sure that other witnesses here today have mentioned the same points but from our point of view this is crucial. The issue is how individuals make choices. Choice is given, which is good, but the question is: how do you make an informed choice? If that choice is not informed, it is a bad choice. What we are seeking to introduce, surely, is better choice, not bad choice. So the question is: what mechanism can you have to allow people to make a good, informed decision? Our real concern with portability and choice of fund is that the mechanisms at the moment are corrupt. They are corrupted by self-interest, generally, in the advice being given, which is profit driven. So people say, 'Let's look at the not-for-profit sector, which is not corrupted by commercial self-interest.' But that has been blighted—it has increasingly been shackled by law and regulation over the years so that it is now impossible for that not-for-profit mechanism to give not-for-profit advice without seeking a licence as though it were a fully profit driven institution.

We have a dichotomy here because an employee or a member of an industry fund—whoever it may be—wants someone to say, generically, in advice, 'Hey, this path of action is probably beneficial.' We would say—and we would fight for it now—that portability would work if you were to allow the not-for-profit funds to give generic advice without licence; that is, without requiring a for-profit type ASIC licence. We have an exemption from the financial services act, which is well received. All we would have to do is extend that exemption to incorporate generic financial advice. I am not saying here that the corporate or its mechanism—the trustee board—executes that advice. The execution advice must be through an ASIC licensed intermediary, who is profit driven.

But at the moment there is no option. There is no choice, in fact, under choice. That is the irony. You have to pay or you have to suffer commissions to get advice. That does not make sense, does it? If we are seeking to protect the best interests of Australians in having the highest corporate governance model, I would suggest or state very strongly that, firstly, the preservation of the not-for-profit structure is the best thing—and it is empirically proven to be—and, secondly, we should allow that mechanism to give generic advice. That would solve the problem of portability in most of its forms.

**Senator CHERRY**—There was one other question I wanted to ask. I am bouncing around a bit; I apologise for that. Does the exemption provided in the regulation for defined benefit funds go far enough, from your point of view, to pick up the sorts of funds you represent?

**Mrs Goddard**—The major issues that we have come across concern the capital guarantees and the investment smoothing, because those sorts of sophisticated mechanisms often occur with accumulation interests in defined benefit funds. I suppose the other issue is generic really. It would be an issue for accumulation funds anyway, but obviously we have a lot of funds which have defined benefit interests and accumulation interests, and the accumulation interests would be portable. Then it just comes down to the question of liquidity, which is an obstacle, because we have funds currently invested on the basis that the money will remain in the fund for statistically predictable amounts of time. The longer those statistically predictable amounts of time are, in general the better the investment returns are going to be. So that is the sort of issue that we are coming across. That is not necessarily a defined benefit issue.

**Mr Brookes**—Perhaps I could raise another point for your information. We have quickly surveyed the membership as to the possibility of portability already existing within the funds. Just to restate, our membership comprises 55 of the larger corporate super funds in Australia, but that represents about \$60 billion, which is over 85 per cent of the whole corporate sector. So it is a small number but they are the heavyweight players. Therefore, when we say our research is based on small numbers, it is based on small numbers of extreme weight of influence.

We are finding, firstly, that—and I will ask Liz to provide some detail—broadly speaking, portability at the moment may exist but it is restricted essentially under trustee governance. Secondly, what is the demand for portability? It seems to be missed at the moment. We saw the way we went charging down a track for free markets, but—

**Senator CHERRY**—I presume it would be restricted according to the SIS triggers, wouldn't it? So once people leave employment there would be no restriction other than with defined benefit funds.

**Mr Brookes**—Correct, but, within that, retained benefits for the large corporates. Mercer were correct in their analysis. For us, we are looking at the large corporates. Retained benefits are provided by about 40 per cent of the membership—if you leave employment you can keep your super fund where it is; that is a retained benefit. That means that there are no commissions and add-on commission based charges attached to it. When you have a free-for-all, the reality of life is that if someone is driven by money—by commission—they will persuade you or seek to persuade you to move from your current zero fee based investment to one that, strangely enough, does attract fees. It is rather clear that that is the inducement for the market mechanisms to follow. At the moment, there is nothing other than those market mechanisms to follow.

This leads to oligopolisation of the market. I know I keep on saying this, but it is true. The signs are there, and it is happening already, whereby the financial conglomerates occupy the key positions around which portability and choice of fund govern the field. To counter that, to have balance, we should have a position where the not-for-profit sector is not eliminated and is not obliged to be for-profit as the only way to survive. The not-for-profit sector itself can give generic advice, dispassionately and disinterestedly, to its members. That to us is the key issue. If we do not cross that bridge, it will be the end of the not-for-profit provision of super and the end of the best deal for Australians.

**Senator BUCKLAND**—Senator Cherry's question went eloquently to where I wanted to go. What are your views on the new 12-month rule?

**Mrs Goddard**—This is a new development in response to the difficulties with having fairly free transfer at almost infinitely short periods of time. We have not analysed it in extreme depth, but it did occur to us that there is a difficulty with the \$5,000 limit, rather than with the 12-month rule. If you make a partial transfer out the trustee can require you to leave \$5,000 in the fund, but if you make an entire transfer out you can take everything. I suppose that 12 months apart you could have two transactions which involve the removal of everything bar \$5,000. I actually could not see the point of the \$5,000, but I have not worked my way through it yet. The 12-month rule goes some way to satisfying the concerns, but annual transfers are still a bit of an issue. But it is not as bad as it was.

**Senator BUCKLAND**—When you do work your way through it, can you provide us with your views?

**Mrs Goddard**—Okay.

**Mr Brookes**—If it helps at all, our initial survey shows that one in 1000, or 0.1 per cent, of members have inquired about portability. We have 750,000 individual Australians who are members of our 55 large corporate schemes. That gives you an idea of the requirement for portability in terms of market demand. There is 0.01 per cent inquiry. How many of those inquiries are converted into action? About one in 10, or 0.01 per cent. So we are 99.99 per cent efficient on that side, and we are bringing in law to cover the 0.01 per cent—at enormous expense.

**CHAIR**—Thank you very much. It is always good to have you here. Thank you for your submission.

**Proceedings suspended from 12.13 p.m. to 1.31 p.m.**

**SHALLUE, Mr Paul Anthony, Member, Superannuation and Employee Benefits Practice Committee, and Chairman, Superannuation and Employee Benefits Practice Committee Legislation Subcommittee, Institute of Actuaries of Australia**

**GALBRAITH, Ms Fiona Anne, Manager, Compliance, Superpartners Pty Ltd**

**CHAIR**—Welcome. We will now form a subcommittee. It is our pleasure to have before us the representative from the Institute of Actuaries of Australia. We invite you to make an opening statement. We would remind you, however, of the amendment regulations that were made two days ago.

**Mr Shallue**—Good afternoon. With regard to the new regulations, we did write to the committee on 12 June setting out a number of concerns with the draft regulations. Perhaps by way of introduction I could say that the Institute of Actuaries does support the principle of providing choice of funds, and we regard portability as one component of this or as an extension of the existing portability arrangements. Our view is, firstly, that a single implementation date for all aspects of choice of fund should apply—that is, choice of fund for new contributions and choice of fund for existing accumulated benefits. Secondly, along with the introduction of that date, one of the key requirements is for an adequate disclosure regime that sets out standardised material which enables ready comparisons between funds, particularly for fees and charges and their impact on benefits.

Perhaps I could turn to some of the details of our submission. I will make a couple of comments, as we go through, about the regulations that were released yesterday, which I have had a quick look at to see to what extent they might address the issues we have raised. The first point we raised was about the exemption of defined benefit components, which we do support. We made a point about the exclusion of benefits where there was a defined benefit component for a member, suggesting that the distinction be made that they were a standard employer sponsored member of the fund. I note that the regulations released yesterday now refer to the member being an employee of an employer sponsor of the fund. I have not checked with colleagues but I think that probably addresses our concern in that area. Our second point was on the definition of ‘defined benefit component’, where we suggested some changes to the wording to ensure that it properly dealt with the range of types of defined benefits that occur.

There was a minor change to the wording in the regulations yesterday, but on my reading I do not think it addresses the issue that we were trying to get to. I am not sure how much detail you would like, but the difficulty is that a common defined benefit is designed to have a resignation benefit, which might be determined as an accumulation type benefit with a defined salary related benefit on retirement. So a defined benefit component may have a withdrawal benefit that is not defined by reference to salary or one of the other items referred to but it may have a retirement benefit component that is. In our view that would still be a defined benefit component.

The second issue we raised was with regard to the surcharge. We see that significant changes will be required to the reporting requirements where there are movements in accumulated balances—that is, when contributions which have been paid within the current reporting year are moved to another fund and yet further contributions are received for that member. There are

issues to be addressed about which fund is to report which contributions, and we think that there will be quite significant changes required to administration systems to deal with that. In terms of the implementation time required for that, we would suggest that fund administrators are probably in a better position than us to address how long those changes might take, but we felt it was appropriate to raise those difficulties.

We then raised an issue with regard to cost implications and we suggested that it would assist funds in controlling costs if the number of transfer requests from any one member were limited to no more than once a year. We are pleased to see in the regulations released yesterday that the trustees are able to restrict the number of transfers to one per year. We also suggested that there be further discretion to allow trustees to refuse requests for partial transfers—that is, that any request should be able to be for the total withdrawal benefit at any one time.

As I read the regulations released yesterday, there appear to be two options that a member can take. They can leave \$5,000 or more in the fund and take out the remainder or they can take the whole of the benefit—that is, they should not leave behind a benefit that is less than \$5,000. That goes part way to addressing the problem which we were concerned about, which is that a small balance might be left. However, it does not address the situation where there would be further contributions with respect to the member. In fact, it probably makes it worse. For example, a member might have been able to leave \$1,000 in the fund. In the next point, we raised difficulties with the loss of insurance cover, for example. One thousand dollars might have been enough to meet the insurance costs for the next few months while new contributions came in, but they are no longer allowed to leave \$1,000; they have to either take it all or leave at least \$5,000. It may actually be counterproductive to the second issue that we raised. Our view is that, where future contributions are to come into the fund, the minimum of \$5,000—if that is the agreed minimum—should remain in the fund.

The next issue was the loss of insurance cover, which I have briefly referred to. We think that is a concern. Although members may be informed about this as one of the issues they need to consider in deciding whether to withdraw a benefit or not, we can see circumstances where people perhaps do not understand what may occur with regard to their insurance cover and may still elect to withdraw the entire benefit and potentially lose some insurance cover.

**Senator BUCKLAND**—Could I interrupt you there because that was one area that I was going to raise with you. I think it is on page 4 of your submission.

**Mr Shallue**—Yes, that is right.

**Senator BUCKLAND**—I am particularly interested in those where, even if the contributions are received, it may be necessary for people to get new health evidence in order to apply for renewed insurance. What happens if you are in a stalled account? Do you come out of it—the account is stalled—and reopen it? Could you take us through that in a little bit more detail. It would save me asking questions at the end.

**Mr Shallue**—Sure. It would depend on the rules of the fund and the arrangements they have with their insurer. It could be that a person is only eligible for automatic insurance cover when they first join and commence insurance cover and if their insurance cover ceases for any reason—for example, there are not sufficient contributions to continue their cover—when the

cover resumes, they would not be commencing employment with that employer for the first time. That might be one of the conditions of eligibility for automatic acceptance—for example, the cover is commencing when they first start employment. That might give rise to the requirement to provide health evidence in order to recommence the insurance.

**Senator BUCKLAND**—Chair, are you happy if I ask just a couple more questions on that?

**CHAIR**—Sure.

**Senator BUCKLAND**—That raises a question about casuals and itinerant workers. Does that apply to them?

**Mr Shallue**—That sort of rule would not normally apply to them. That sort of rule would more commonly apply to an employer sponsored plan for regular employees. For example, often with casuals you would find that they would not be provided with disabled cover, whereas permanent employees would be provided with disabled cover. Different insurance contracts and arrangements generally apply to permanent employees.

**Senator BUCKLAND**—‘Casuals’ was not a really good choice of word. Some industries that I have contact with have now started the practice—and let me put it on the record that I opposed that move at the time—of getting permanent employees on a casual basis. They say, ‘We have a peak load and we’ll need you for maybe six or 12 months or even two years.’ They are deemed to be permanent for the period they are there. They get all the entitlements of a permanent employee. Quite a few of them then just sit around—they have taken packages and are just doing something when it is available—and do not go back into the work force as casuals in other jobs; they just wait until they get another go in these particular plants. They are plants that have had reductions in work force numbers and just bring in staff for peak loads, generally through labour hire people. But while these casuals are there they are permanent employees. Would this affect them?

**Mr Shallue**—Again, you would need to come back to the specifics of the insurance arrangement for the particular fund that they are in. You would hope that the insurer and the trustee would be able to come to an agreement about how to maintain cover for those sorts of people.

**Senator BUCKLAND**—I might make inquiries on that because it is a very interesting point.

**Mr Shallue**—It is quite a common arrangement, particularly in employer sponsored funds for permanent employees. What is called automatic acceptance only applies if someone joins the fund and takes up the insurance when they are first eligible, which is when they join the service of the employer.

**Senator BUCKLAND**—They are pretty large employers—what we would categorise as large employers. Despite the fact that casuals come in under labour hire arrangements, they are actually paid by and pick up the benefits of the employer, not the labour hire company.

**Mr Shallue**—Is that only for the period for which they are employed?

**Senator BUCKLAND**—It is only for that period.

**Mr Shallue**—So they might work for two months.

**Senator BUCKLAND**—Yes. They might have two months employment this year, but the employer might get a big order next year and want them for a couple of years. So in that intervening period they have stalled employment. It is perhaps something that I need to pursue myself.

**Mr Shallue**—It would be worth inquiring into, because insurers would often not be comfortable with continuing insurance cover for people who may—for example, if they are not working for that particular employer during a three-month period—go off and do other things which may present a different risk.

**Senator BUCKLAND**—Some do but quite a few do not. They wait only for that employment. I am also interested in them having to do a further medical test, because I understood they did not; I understood they just had to have a security pass into that environment.

**Mr Shallue**—Yes.

**Senator BUCKLAND**—Thank you for that.

**Mr Shallue**—I shall move on to the partially vested arrangements. These arrangements were probably more common in the past but there are still a number of employer sponsored schemes which provide benefits in excess of superannuation guarantee contributions and have accounts which are only vested over a period which might be five or 10 years. The regulations, as we read them, apply to the withdrawal benefit. For example, the withdrawal benefit might be \$18,000 and the total account balance might be \$20,000, so the question is: if I withdraw my \$18,000, do I lose the whole \$20,000 or is there \$2,000 left there? If so, what happens to that \$2,000 and what rules apply to that? So we are raising an issue with regard to those unvested accounts which trustees and employers will need to consider and come up with rules for. Members will need to take those rules into account in deciding whether or not they transfer out balances from those sorts of arrangements.

**CHAIR**—But they still have those situations though where they have left the employment?

**Mr Shallue**—No, because normally the vesting will depend on the period of service up to when service terminates.

**CHAIR**—Defined benefit funds are now excluded, so how do we run into your problem if they are now excluded and there is not a problem in terms of an inactive account?

**Mr Shallue**—Because the regulations apply to active accounts as well as inactive accounts.

**CHAIR**—Yes, I see, because it is possible for a person to use portability in terms of an active account. Thank you for clarifying that.

**Mr Shallue**—The next item we raised was the disclosure item, which I mentioned briefly before. We consider the disclosure requirements with regard to choice of fund for existing account balances to be similar to those for choice of fund for new contributions. We think it is important that there are standard disclosure requirements which it is agreed are appropriate to members making decisions on those issues. Hence the next point, which was that we regard it as appropriate to have a single implementation date for movement of existing account balances and choice of fund for new contributions.

The last point that we raised was whether there was a need for some protection for trustees and employers against the possibility that a member who is not happy with the decision that they made to transfer a benefit out subsequently goes back and tries to sue the employer or the trustee for allowing them to make a choice which subsequently turns out to be inappropriate. In the updated regulations I cannot see anything that is dealing with that. In fact—and I am not sure whether there was a change—I find it interesting that regulation 6.34(2), which deals with the information required, says that, before the trustee or regulated super fund or an approved deposit fund rolls over or transfers the amount, the trustee must be satisfied that the member (a) is aware that ‘the member may ask the trustee’ for various information on fees and charges et cetera and (b) does not require such information. I think that is an interesting one for trustees to consider. For the trustee to ‘be satisfied’, is that a matter of getting a statement from the member saying, ‘I do not want any information’? If I were a trustee I am not sure that, if a member told me that they did not require that information, I could be satisfied that they did not, because my view would be that they did require information in order to make that sort of decision.

I wonder whether there are any sleeping issues there for trustees in terms of liability. We think some consideration needs to be given to that. On those sorts of issues, we would defer to the lawyers as to whether or not there does need to be some protection there. They are my comments on behalf of the institute. However, on that last point, they are my own views and I have not passed them by anyone else in the institute. But I think we did raise the issue of protection for trustees and employers, and I suspect it is still an issue that needs to be thought about.

**CHAIR**—The committee also has a letter from the Institute of Actuaries of Australia dated 17 February 2003, signed by Chris Lewis. I know lots of things have happened since then. Do you have a copy of that?

**Mr Shallue**—Yes.

**CHAIR**—Could you comment on item 3 on the third page of the letter to Mr Kennedy from Treasury.

**Mr Shallue**—That mainly relates to issues that would arise if defined benefit components were allowed to be transferred.

**CHAIR**—So that really is not relevant now?

**Mr Shallue**—No, it is not relevant now.

**CHAIR**—That is what I wanted to check. Thank you very much for that.

**Senator BUCKLAND**—Following the comments the committee heard this morning on the surcharge, I note that you also have some comments in your document about that. Would you like to expand on that matter?

**CHAIR**—Just on that, the representative from Mercer felt that some of them were almost incomprehensible and that he would need to discuss it with colleagues and others to try and get a feeling for what the intention was. Did you have that sort of trouble?

**Mr Shallue**—Are we talking about the surcharge regulations themselves or the implications for portability?

**CHAIR**—No, we are talking about the final regulations that were released about two days ago. Some of them are clear in terms of the 12-month rule, but there are other areas where there has been some difficulties. I am referring to Mr Ward's comments. He had trouble understanding what the Treasury officers who promulgated those regulations were going to achieve. Ms Galbraith, you might be able to help us.

**Ms Galbraith**—I think Mr Ward had an issue with how the \$5,000 was going to work in conjunction with the 12-month rule. He also had an issue with the same regulation that Mr Shallue and I have an issue with, which is the new information disclosure provision—6.34(2). It is not very clear at all how that will work in practice, and I have the same concerns as Mr Shallue. It looks as though it is an objective test and the trustee has to decide whether or not the member requires the information—an impossible test to satisfy. It really should be whether or not the member has declined the information. The other issue raised was also in respect of the surcharge, which I think is the same kind of issue that Mr Shallue touched on—that is, the issues that will be involved in administering a surcharge when there are part payments in the system. It is not something that Superpartners has an issue with because we currently have part payments and our system is configured to handle it. But a lot of corporates do not have that kind of mechanism in place. Mr Shallue would be more appropriate to talk about that. Trying to deal with the interaction of portability with part payments if people do not take the whole amount but only take part of it and how that will link in with surcharge is one of the major issues he raised this morning as well. That might be something you touched on I think, but it is for you to elaborate on.

**CHAIR**—Thank you for your assistance. Does that throw a bit more light on the dealings with which one of your colleagues had some concerns?

**Mr Shallue**—Yes, I think it is the same issue. For example, if there is a \$20,000 account balance and someone takes out \$10,000 of that, with regard to the contributions of \$5,000 which have been received for that member so far for the year, does the \$5,000 go out with that \$10,000 withdrawal or does that \$5,000 stay in the fund? Or does half of it go and half of it stay because half of the benefit was withdrawn and half left behind? Who is responsible for reporting the \$5,000 of surchargeable contributions in the first six months? Is it the fund that the money was transferred to, the fund that the money was transferred from or do each of them have to report part of the \$5,000 in surchargeable contributions? Rules around how that is to operate need to be established before funds can satisfactorily administer the transfer of benefits and the surcharge regulations.

**Senator BUCKLAND**—I am sorry I put you on the spot with that but it happens. I am interested and concerned about the amount of money that has been spent to date to set up a system where you can cope with the requirements. Is it likely that you are going to have to spend more to cope with any changes that come in as a result of these regulations?

**Mr Shallue**—Certainly. Fund administrators will need to spend money to change their systems to properly allocate the contributions to the partial payments that are going and what remains in the fund. So, yes, there will be requirements to update systems and administration procedures.

**Senator BUCKLAND**—Are we talking about a couple of thousand dollars or are we talking about another figure?

**Mr Shallue**—With surcharges you are never talking about a couple of thousand dollars.

**Senator BUCKLAND**—No—for setting up a system.

**Mr Shallue**—I think significant costs would be involved. I defer to the fund administrators as to what that might be.

**CHAIR**—We understand that currently the tax office will not accept information on partial payment electronically. It must be done manually. So that will cause some problems, I think.

**Mr Shallue**—I am not involved in the actual administration side of things. I am more on the actuarial side so I cannot comment directly on that, but I am not surprised at that comment.

**CHAIR**—Thank you very much. I always appreciate a contribution from the Institute of Actuaries. For many years you have been very helpful.

[2.05 p.m.]

**RUBINSTEIN, Ms Linda Esther, Senior Industrial Officer, Australian Council of Trade Unions**

**CHAIR**—Welcome. We welcome your submission on behalf of the ACTU and invite you to make an opening statement. Are you aware of the changes that were made to regulations two days ago?

**Ms Rubinstein**—Yes, I am. I received them yesterday.

**CHAIR**—They may or may not influence some of your earlier comments. The floor is yours.

**Ms Rubinstein**—Thank you. The ACTU welcomes the opportunity to make a submission to the committee in relation to the portability regulations. At the outset, I would say that the ACTU does support portability of superannuation; that was one of the issues unions addressed in the 1980s when they contributed to the establishment of industry funds. Portability was a key issue prior to that. Employees who left their employment before retirement age all too often had to leave their superannuation behind and, if they did receive any benefits, would not receive those until retirement age and could well end up with superannuation that had been effectively left behind for 20 or 30 years.

The concern with the regulations, however, is that they appear to facilitate, if not encourage, transfer from an employee's active fund—that is, the fund to which employers are currently contributing. That is not something that we believe ought to be encouraged or facilitated, particularly through the device of regulations, when the issue of choice itself has not been resolved by the parliament. As you would be well aware, a number of issues of concern—in particular, issues in relation to education, disclosure, the role of financial planners et cetera—have been identified with the choice legislation. These regulations would permit financial planners, banks and other promoters, particularly those of retail products, to market those to people who are currently members of employer sponsored superannuation funds—whether they be corporate funds, industry funds or public sector funds—and say to them, 'You can transfer from that fund from time to time into these other products.' The very same problems that apply to the choice legislation apply in this case because the conditions governing disclosure of fees, charges and other relevant matters have not been finalised to the satisfaction of the parliament.

The amendments to the regulations, although seemingly directed at addressing some of these concerns, barely touch the real issues. The imposition of a \$5,000 limit if there is only a partial transfer to be taken would appear to be doing a couple of things. First of all, it would ensure that people who are fairly well-off would be targeted by this measure, because many ordinary Australians do not have superannuation accumulations much more than \$5,000. It is perhaps also directed at the concerns of some funds, in relation to insurance arrangements and other matters, if only a small residual amount is left in the fund. It spreads administrative costs over the whole of the fund membership. It is difficult to see the rationale, however, for a \$5,000 limit, or any limit really. Without knowing the reasons, one can only speculate.

The provision allowing for such a transfer to occur only every 12 months is presumably also aimed at addressing concerns about effects on administration costs, liquidity, insurance and so on. But the real question that has to be asked is: ought this to be the case? Ought choice in effect be promoted in this way through regulation, seemingly as a device to get around the problems which the choice legislation itself has had in the parliament? The answer, we would say, to that is no.

The amendments to proposed regulation 6.34(2) really do not go any way towards the kind of disclosure and information that would be required. All that this would seem to require is that a member transferring would have to be told that they have a right to certain information about the costs of that, without being told what form the information is in or being given the information. Of course, as we know, the way in which people are given information and the way in which it is structured is absolutely critical to their understanding. We certainly have not as yet found the right way of doing that in respect of superannuation.

We welcome provisions that are directed towards preventing funds into which employees are no longer receiving contributions from refusing or delaying unduly requests to transfer those funds in order to allow the member to consolidate multiple funds into an active account. These regulations go well beyond this to the issue of making employees very vulnerable to approaches to regularly transfer from an active fund to another active fund, thereby leaving them in a position where they are paying multiple fees and being confused about insurance. As you are aware, you cannot be insured twice, and they might well be paying two lots of insurance. We also have other issues. However, there seems to be nothing in these recommendations that ought to commend themselves to the Senate.

**CHAIR**—There is a time frame of 90 days for executing a transfer—do you think that is too long?

**Ms Rubinstein**—In the submission we have said it is too long. We said that it ought to be possible to process these transfers, assuming all the information has been received, within 30 days. To tell the truth, it ought to be able to be done much sooner. Certainly benefit payments and normal contribution processing are done much sooner by the administrators. While setting a time limit is a good thing, certainly it is difficult to see from an administrative point of view why 90 days would be required to effect such a transfer.

**CHAIR**—You believe the regulations are adequate in terms of where the fund is chasing an employer for some outstanding contributions to exceed that 30 days—or 90 days as is at the moment.

**Ms Rubinstein**—Sorry, I am having difficulty because I cannot see you because to the light. Could you repeat your question? You are just a—

**Senator BUCKLAND**—'He's a flash in the pan,' I think is what you were going to say, was it!

**Ms Rubinstein**—No. That is much better, thank you.

**CHAIR**—It was put to us this morning that generally it was felt that there are adequate protective measures in the regulations to cover cases—beyond 90 days at the moment—where the fund is chasing a delinquent employer for past contributions. Do you agree with that?

**Ms Rubinstein**—We have not really considered that. Are you referring to these regulations?

**CHAIR**—Yes.

**Ms Rubinstein**—Normally funds will chase delinquent employers.

**CHAIR**—That is right. The point is that, in the situation where funds are chasing the employer, you might go beyond the 30 days—your 30 days—or you might go beyond the 90 days.

**Ms Rubinstein**—Yes.

**CHAIR**—Are you satisfied that there is enough protection there in terms of reasons for the delay?

**Ms Rubinstein**—I think that that is probably the case if it is something that is not within the fund's power. What is very important is the way in which funds actually do take up the arrears collection process. I believe most funds—certainly the industry funds—would begin that process within a very short period of the contributions being overdue.

**Senator BUCKLAND**—You made mention of the regulations, and I am wondering if you, or anyone, can help me with that. On transferring there is a requirement that the transferring member of a fund is told about the funds that are withheld, they are told about the funds they are taking, what is happening and the costs associated with that, but there does not seem to be anything in the regulations, unless you can tell me otherwise, to say that they will be told—and they will not be told—that they are going to lose their insurance cover and things like that. I do not know if you can see anything, Chair. Certainly I cannot see it in the regulations.

**Ms Rubinstein**—Unless insurance is a benefit entitlement, and I think that is the case.

**Senator BUCKLAND**—But that could sway a lot of people, don't you think?

**Ms Rubinstein**—I think it is a key issue, but I think the issue is bigger than just putting insurance arrangements in this. I think this is not the way. Paragraph (2) of that regulation is not anything like an adequate way of dealing with the need for disclosure both in relation to the fund from which the employee is transferring and in relation to the fund to which they are transferring, which are of course related issues.

**Senator BUCKLAND**—I think I would agree with you, but I would say it is totally inadequate. It seems to me that we are only going to be telling people half the story.

**Ms Rubinstein**—I think insurance is one of the key issues—that is right. It may well be that people are told, 'You'll keep your insurance if you are an active member of the fund.' I think that is what we are really talking about. If they remain an active member of the fund, they will still

be paying the insurance but they will also of course be paying two lots of administration fees. The concern also comes with the fund to which they are transferring. Do they know what the insurance arrangements are in that case and do they understand that, if they are paying for two lots of insurance, they do not get two lots of insurance should something happen?

**CHAIR**—What constitutes an inactive account? Do you perceive that there perhaps is a need for a 12-month rule to determine an inactive account, to cover casual workers and seasonal workers?

**Ms Rubinstein**—Most funds have definitions of inactive accounts and they will generally be accounts that have not received contributions for perhaps six months or 12 months. That is just where nothing happens—nobody notifies anybody of anything. But, if an employee ceases employment with one employer and goes to work for another employer and that employer is contributing to a different fund, the employee ought to be able to transfer their accrued benefits from the first fund to the second fund. There is no argument about that. They would say, ‘I have ceased employment with that employer,’ and, in effect, ‘Contributions will not be coming.’ If there is a 30-day or 90-day period, in any event the truth of that statement will be more or less clear. So, in itself, that should deal with it. There will be exceptions, but that would be the way that you would see it working. The problem is really where people are in a superannuation fund and they believe that, for whatever reason, they should have another fund which, from time to time, they will transfer to from the first fund, although they will still remain a member of the first fund.

**CHAIR**—Yes, we can see major difficulties there.

**Ms Rubinstein**—Absolutely. First of all it encourages a multiplicity of funds, with all of the problems that you know as much about as we do, or more than we do. Secondly, it actually nullifies, by regulation, something that the parliament has not been prepared to agree to—it nullifies the real effect of industrial instruments, awards and agreements that specify the fund that employers will contribute to. It gets around that because the employer will contribute to it—and that is a decision that has been made—and the employee will keep taking the money out. I do not think that it is going to be of such a scale that it is going to damage the funds, but I think it is potentially of great damage to the employee, without any of the proper regulations in place to ensure that they are not disadvantaged and that they know what they are doing.

**CHAIR**—Actually the Senate has power to disallow regulations.

**Ms Rubinstein**—I understand that.

**CHAIR**—So our report will be going in before that deadline.

**Ms Rubinstein**—I guess that is my point—should the regulations not be disallowed, a form of choice of fund will be put in place, with none of the issues resolved which the Senate has said it wants resolved before it is prepared to pass the choice legislation. That is the concern.

**CHAIR**—Thank you very much, Ms Rubinstein. We had a very comprehensive presentation by one of your colleagues first thing this morning and we do not have to ask the same sorts of

questions of you because they have been covered. Thank you very much for what you have added to the debate today.

**Ms Rubinstein**—Thank you.

**CHAIR**—And I apologise for Senator Sherry, who reported in sick today.

**Ms Rubinstein**—I am sorry to hear that.

[2.28 p.m.]

**KELLEHER, Ms Noelle Eileen, Member, Superannuation Centre of Excellence, Certified Practising Accountants Australia**

**CHAIR**—Welcome. We look forward to your oral presentation. It does not necessarily have to be too brief. Because as it is towards the end of the day, a lot of the issues we were worried about have been answered by some others so, rather than repeating the exercise, we are now looking for new information and new insights.

**Ms Kelleher**—That could be interesting.

**CHAIR**—That is the challenge.

**Ms Kelleher**—CPA Australia and its Superannuation Centre of Excellence are happy to participate in the public hearing in relation to the portability of super benefits. In principle, CPA Australia supports portability but recommends that it be done in conjunction with choice of fund so that it does minimise the burden on superannuation providers and employers where appropriate.

In addition, we recommend that portability and choice be implemented once there has been an adequate member education program undertaken. The program needs to be a comprehensive government funded program because superannuation providers do not have the educational skills required to achieve such a program, and it could raise a lot of FSRA licensing issues if the trustees of funds et cetera were to undertake such an education program. Any program that is implemented needs to be impartial and unbiased. It needs to be free of political messages and any products for sale et cetera, so that members actually understand the implications of portability.

CPA Australia has been quite concerned about the way in which portability has been introduced. As indicated in our submission, portability and choice should be considered together as a single legislative package. Portability as it stands represents a de facto choice of fund regime, and we have been extremely disappointed by the fact that the regulations have been introduced while the hearings have been taking place. While we understand the government's motives in doing this to try and clear up some uncertainty and to give funds a bit of time to get their affairs in order in terms of how they are going to manage portability, we believe that it actually creates more uncertainty as to how the Senate findings will feed into the regulations as they stand at the moment, whether various submissions have actually been taken into account et cetera. CPA Australia has been concerned that the regulations have been introduced while this whole consultative process has been taking place.

**CHAIR**—Thank you very much. Can you see any very significant impediments to members' benefits or members' rights?

**Ms Kelleher**—In terms of impediments to members' benefits or rights, if they understand the implications of what they are choosing to do then there are probably no impediments. But that is

on the basis that they actually understand the ramifications of what they are doing in terms of what it means for insurance cover and investment choice, what it means from a fee and charge perspective and whether they are actually going to end up being in a neutral—or, in theory, better—position at the end of the day. It really is all dependent on whether they actually understand what they are doing.

**CHAIR**—Are you in favour of an industry or APRA standardised document for an application for transfer?

**Ms Kelleher**—There needs to be one. If the portability regime is done on the basis of ad hoc documents and ad hoc considerations of any requests for suspension of transfer requests et cetera then that is going to lead to problems arising because it is not a transparent process. There needs to be a standard form. There needs to be clear understanding of what the new funds which get the transfer benefits need to do in terms of working out whether the transferred benefits can be paid at some later date because the member has triggered the payment of their benefits because they have terminated employment et cetera. In terms of applications to APRA, where the trustees are trying to suspend a benefit payment or benefit transfer there needs to be knowledge of what significant grounds for considering those things are and what different things APRA looks for, the information they need et cetera.

**CHAIR**—Do you think that document should have a checklist which asks the member whether that member understands the consequences of the transfer in terms of the possible implications on his insurance cover? Should it list as separate items insurance cover, the cost of exit and other relevant matters?

**Ms Kelleher**—Anything that can go into a checklist form is a good thing, bearing in mind that you need to be able to determine whether the responses you are getting back actually mean anything. You can ask someone if they understand they are losing their insurance cover, and if they say yes there is a question as to whether that is a real yes and they do understand or whether it is not and they do not.

**CHAIR**—So we need real yeses.

**Ms Kelleher**—Real yeses and real noes. Being told what is going to happen, or what could happen, as a consequence of what they are doing is different to actually understanding it. In the regulations that have been introduced, regulation 6.34(2) says that the trustee of the fund that the benefits are coming out of must be satisfied that the member knows that they are able to ask for information to do with the implications of their benefit entitlements in relation to portability. They also have to satisfy themselves that the member does not require that information. Even from a trustee's perspective, how do they know that the member does not need the information that they are being given, or that the trustee wants to give them, et cetera? A checklist may ask, 'Do you understand what is going to happen?' but that still leaves open whether it is a real yes or a real no.

**Senator BUCKLAND**—What it really comes down to is that we seem to be making regulations quickly and hastily, without really considering the impact they may have on superannuants and their ability to understand what is occurring around them. How do you know a real yes? How do you know a real no? Needs at that moment will determine the strength of the

yes or no—'Yes, I understand it because I want to get out of here quickly' or 'Yes, I understand what the implications are for a period of time and that I am not going to have insurance.' I do not know how you would tackle that.

**Ms Kelleher**—I do not know how you would tackle it, except that you do not rush into portability—trying to get it up and running by 1 July—if you have not already started a very clear campaign explaining what portability means and without getting into the political messages of 'this is great' and so on. You actually have to get down into what it means in terms of your existing entitlements and your existing investment choice. The fact is that super is a long-term investment. Just because you have had a poor return for this 12 month period does not mean that you are not going to get absolutely wonderful returns for the following two, three, four or five years, when you start looking at the long-term horizons. Going into portability without having an appropriate education campaign that is unbiased et cetera is just asking for trouble. I think there will be people who, rightly or wrongly, end up in the position where they are chasing short-term gains—or, rather, their advisors are. I do not even know whether it would get down to the individuals chasing the short-term gains; it will be other people chasing them, and perhaps not even for the member.

**Senator BUCKLAND**—I can relate an experience that I have had only in the last six weeks. I was determined to take some superannuation out of a fund it is in at the moment that I had accumulated before going into the Senate. I felt sheer anger at the way I was treated when I was trying to get answers to certain questions. I found out that I had to pay in excess of 20 per cent in exit fees. But I think someone on a shop floor or sitting in an office all day might not understand the implications of that. I was in a better position because I have super now, but some of those people are moving funds simply because they think they will get a better deal somewhere else when in fact they are negating it all. It is a terribly difficult question, isn't it?

**Ms Kelleher**—It is a very difficult question, and all I can say is that if you look at your own position where you are a well-educated person and have a bit of a financial background—

**Senator BUCKLAND**—Don't build that part of it up too much!

**Ms Kelleher**—I am not buttering you up but I am saying that if you look at your experience in life in terms of your background, exposure to financial matters and your awareness of some of the issues and yet you are feeling as though you have had difficulties, then imagine the situation an ordinary person who does not know what sort of questions to ask et cetera could end up in, simply because they do not even know to ask the questions about fees, choice and insurance—'Will my insurance be at different levels; will it be for different things; how long will temporary cover et cetera be paid out for?' If you have no idea of those questions then how do you make a comparison with the fund that you are in, where you have potentially got a good benefit and good returns to be expected as you approach retirement?

**Senator BUCKLAND**—I think the drafters of the policy have never been in the situation where they sit in front of a financial adviser, where the financial adviser is painting a very glossy picture of what they will get for you but they forget to tell you what you will lose and what they will get for themselves. I must say that I am a bit critical about that. I am very concerned about this, because I do not think that people understand the impact of what we are talking about.

**CHAIR**—Thank you very much, Ms Kelleher. I thank the Superannuation Centre of Excellence for its submission and for providing you with the time to come. It is much appreciated.

**Subcommittee adjourned at 2.41 p.m.**