

22 August 2012

Mr Ross Jones
Deputy Chairman
Australian Prudential Regulation Authority
Level 26, 400 George Street
Sydney NSW 2000

Dear Ross,

Risk Disclosure

We are writing to express our serious concerns about the labelling, form, and potential uses of the “Standard Risk Measure” (SRM), defined by APRA as the expected frequency of negative annual returns over a 20 year period.

Recent Government policy statements and draft consultation documents indicate that the SRM will be included in the new APRA data collection and the MySuper product dashboard.

We recognise that there is a clear need for consistent descriptions of risk, and that no single measure of risk will be perfect. Nonetheless, it is apparent that the measure can be improved on and, if adopted in official communication, will take years to recast.

We note that in some contexts the SRM has been suggested for use on an “if not, why not?” basis, allowing room for alternate presentations of risk. While such flexibility is advantageous, it potentially undermines the goal of industry-wide consistency, and is not an effective argument against efforts to make the measure stronger if possible.

We consequently suggest that, before APRA and ASIC begin to utilise the SRM, they consult with industry directly, including on the following issues:

1. Labelling

The measure’s current label suggests that it gives a general indication of investment risk. In fact, the measure captures annual downside volatility, expressed over a 20 year period. This misrepresentation may be against the member’s interest. We strongly recommend that the measure be renamed, and suggest “Volatility Rating” or “Downside Risk Measure”.

2. Calculation/methodology

The SRM calculation methodology offers limited guidance and in particular does not provide for standardised assumptions about the risk and return associated with key asset classes. There is consequently no guarantee of consistency in the numeric rating of products. The appropriate presentation of returns also remains a contentious issue across the industry.

3. Enhanced investment risk measures

The initial APRA communication on the SRM was focused on assisting consumers make like-for-like comparisons. However, annual volatility may not be the best general risk measure for superannuation – a retirement savings vehicle with a legislated long-term investment horizon.

The use of a downside volatility measure without full explanation and without the use of other risk measures would be expected to encourage more consumers to reduce volatility, and therefore long-term expected returns.

A number of superannuation funds and industry bodies have already started to consider a range of alternatives, including:

- the range of potential retirement balances over 5, 10, 20 or 40 years; and
- the likelihood of meeting specified short term (5 year) and long term (20 year) investment goals.

We recommend that APRA establish a formal process for the development of enhanced measures, and announce this in the forthcoming discussion paper on data collection. We are also concerned that where a particular risk measure is mandated by the regulator (even on an “if not, why not” basis) this needs to be supported by adequate legal protection for trustees.

We are committed to working together with the whole of the superannuation industry, both as an industry and with Government, in pursuit of the recommendations made in this letter and other outcomes consistent with the core requirements of the Stronger Super reforms.

We would welcome the opportunity to discuss this letter with you and your colleagues.

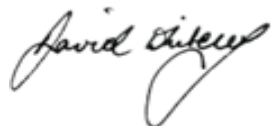
Yours sincerely,



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David Whiteley
CE