2 October 2012

Committee Secretary
Parliamentary Joint Committee on Corporations and Financial Services
PO Box 6100
Parliament House
Canberra ACT 2600

By email to: **corporations.joint@aph.gov.au**

Dear Sir,

Senate Inquiry into Superannuation Legislation Amendment (Further MySuper and Transparency Measures) Bill 2012

The Actuaries Institute is the sole professional body for actuaries in Australia, providing independent, expert and ethical comment on public policy issues where there is uncertainty of future financial outcomes. It represents the interests of over 4,000 members, including more than 2,100 actuaries.

Some of the principles that guide the Actuaries Institute's inputs into public policy are:

- Acceptance of public sector involvement where the market does not meet societal needs.
- The need to take a long term policy view, with appropriate transitional arrangements.
- Ensuring that consequences of risk taking behaviour are borne by the risk taker.
- Issues of intergenerational equity.
- Clear and reliable information available for decision making.

The Actuaries Institute welcomes the opportunity to submit comments on the *Superannuation Legislation Amendment (Further MySuper and Transparency Measures) Bill 2012*.

The Actuaries Institute has, over the past six months in particular, made a number of submissions to Treasury, the Productivity Commission, and the Australian Prudential Regulation Authority ("APRA") regarding fees and costs and investment performance for superannuation funds. Dialogue with APRA is continuing.

We are disappointed to find that the concerns we raised in our submission to Treasury of 16 May 2012 regarding the Exposure Draft of this Bill have not been addressed. We urge the Committee to consider this submission, along with our 1 August 2012 submission to the Productivity Commission's call for feedback on the Default Superannuation Funds in Modern Awards Draft Report, and **enclose** a copy of each submission with this response.

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Net Investment Returns

We note that the Bill requires APRA to publish the "net return" in respect of each MySuper product. The definition of "net return" has not been set out in the legislation. Therefore it will be APRA that will determine how this important information will be calculated.

APRA has recently released a *Discussion Paper on the Reporting Standards for Superannuation (19 September 2012)*. In this document, APRA have indicated that "net return" will be "net investment return" less administration fees. The Actuaries Institute has, in a number of recent submissions, highlighted the potential for this approach to lead members into making decisions that are not in their best long term interests. Our concerns can be summarised as follows:

1. If administration fees are deducted from the net investment return to obtain the "net return", members may incorrectly interpret the result as providing some insight into the investment capabilities of their superannuation fund. Clearly, only the net investment return will provide any such insight.

2. In assessing whether or not the level of administration fees provides good value to a member, the member must consider the level of these fees having regard to the level, quality and timeliness of the administration services provided to the member. Comparing superannuation funds based on a "net return" that has been reduced by administration fees provides a member with no help in this analysis. In fact, it may confuse the member.

The Actuaries Institute is concerned that the methodology followed by APRA may lead members to assume that superannuation funds with the highest net returns have the best investment expertise. This may be the case for some superannuation funds. However, for other funds, it may simply be that their administration fees are lower and this may mask the fact that their investment performance is worse than some other funds with lower net returns.

As it is the net investment return that is the major influence on the final retirement benefit of a member, a member who selects such a fund may be disadvantaged.

The Actuaries Institute is also concerned that this may lead members to choose a superannuation fund that increases its net return by reducing its costs by reducing the extent, quality and timeliness of its administration services.

Calculation of Administration Fees

As explained in our submission to the Productivity Commission, expressing administration costs as a percentage of the value of fund assets is unsound and may mislead members.

For example, consider two identical superannuation funds with the same membership and fee structure, but where one fund started five years after the other. The newer fund will have lower assets and hence a higher administration cost percentage, yet its fees are the same as the older fund.

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The Actuaries Institute therefore recommends that the Bill be amended to change the reference to "net returns" on page 51 to "net investment returns" and to delete both sub-clauses (2)(e) on pages 27 and 28 of the Bill.

We would be pleased to discuss the issues raised in this submission or to respond to specific questions to assist the Committee in the course of its work.

Please do not hesitate to contact Andrew Boal, Convenor of the Superannuation Practice Committee, on (03) 9655 5103 (Andrew.boal@towerswatson.com) or Chief Executive, Melinda Howes, on (02) 9239 6106 (melinda.howes@actuaries.asn.au) if there is any way we can assist.

Yours sincerely

David Goodsall
President

Enclosed:

Letter to Treasury, Superannuation Legislation Amendment (Further MySuper and Transparency Measures) Bill 2012 Exposure Draft, 16 May 2012.

Letter to the Productivity Commission, Response to Default Superannuation Funds in Modern Awards Draft Report, 1 August 2012.

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16 May 2012

The Manager
Superannuation Unit, Financial System Division
The Treasury
Langton Crescent
PARKES ACT 2600

By email to: strongersuper@treasury.gov.au

Dear Sir

Superannuation Legislation Amendment (Further MySuper and Transparency Measures) Bill 2012 (Exposure Draft)

The Actuaries Institute ("the Institute") is the sole professional body for actuaries in Australia, providing independent, expert and ethical comment on public policy issues where there is uncertainty of future financial outcomes. It represents the interests of over 3,800 members, including more than 2,000 actuaries.

Some of the principles that guide the Institute's inputs into public policy are:

- Acceptance of public sector involvement where the market does not meet societal needs,
- The need to take a long term policy view, with appropriate transitional arrangements,
- Ensuring that consequences of risk taking behaviour are borne by the risk taker,
- Issues of intergenerational equity, and
- Clear and reliable information available for decision-making.

The Institute welcomes the opportunity to submit comments on the Exposure Draft of the *Superannuation Legislation Amendment (Further MySuper and Transparency Measures) Bill 2012*.

The Institute has, over the past six months in particular, made a number of submissions to the Australian Prudential Regulation Authority ("APRA") regarding fees and costs and investment performance for superannuation funds. We hope to have the opportunity to discuss these with APRA in the near future.

Proposed Section 1017BA of the APRA Act 1998

An aspect of the Exposure Draft which concerns us is that there are a number of references to a period of "10 years". We consider that in developing the finer details of the information to be collected and published it may prove too rigid to specify a 10 year period in legislation. The approaches that best assist members of superannuation funds to understand the investment performance of superannuation funds are currently being developed. In this process, it may be found that information for periods other than 10 years is more informative.

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We refer you to the enclosed submission dated 13 April 2012 where one of the proposals we have developed for investment performance uses earning rates over three consecutive four-year periods, aggregating twelve years in total.

We believe that legislation should not constrain the development of new approaches that better inform members.

We therefore recommend that the references to this period be changed to either:

(a) "10 years (or such other period or periods as are specified in the regulations from time to time)", or

(b) "such period or periods as are specified in the regulations from time to time".

We consider this flexibility is desirable both initially and in the future as sound practices are developed and improved. We also note that alternative (b) above is consistent with the proposed Section 29QB(1)(b) of the *Superannuation Industry (Supervision) Act 1993*, and paragraph 3.51 of the Explanatory Memorandum, relating to information to be published on the public section of superannuation funds' websites.

Allowing our proposed approach and other proposals to be considered, implemented and improved over the years will be less difficult if the period can be varied by changes to a regulation rather than to legislation.

This flexibility would allow the development of better measures without altering the basic principles in the draft legislation.

Proposed Section 348A of the Superannuation Industry (Supervision) Act 1993

We presume that the intention of this new section is to require the publication of information that will allow the comparison of costs and investment returns across different MySuper products and providers. To achieve this it will be important that the material published takes into account the relative size of the membership and assets which relate to each MySuper product.

We therefore recommend that sub-paragraphs (1)(a) and (1)(b) have the words "annual rate of" inserted before "fees" and "costs". These "annual rates" could, for example, be expressed as an amount per member (for administration fees and costs) or as a percentage of assets (for investment fees and costs). For consistency, it would seem preferable if sub-paragraph (1)(c) also had the words "annual rate of" inserted before "net returns".

Our views on how these "annual rates" should be determined have been set out in various submissions that we have sent to Treasury, APRA and the Productivity Commission ("PC"). The most recent are:

31 May 2011	to Treasury	Investment fees and costs
13 December 2011	to APRA	Administration fees and costs
16 April 2012	to APRA	Investment returns
13 April 2012	to PC	Fees, costs and returns

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We would be pleased to provide copies of these but we assume that details about how such "annual rates" should be determined will be set out later in the Regulations.

Finally, we refer to sub-paragraph (1)(c) specifically. This sub-paragraph will require APRA to publish "the net returns to beneficiaries". When considering the way that investment earnings are allocated to the accounts of superannuation fund members (i.e. beneficiaries), it is important to understand that:

1. Such allocations are achieved by a wide range of methods. Some funds use unit pricing to achieve this. Other funds declare crediting rates that apply for a period such as one month. Very few funds use an annual rate to allocate investment returns to beneficiaries. This will mean that, for most funds, there will not be one rate that will apply to all members for the fund year. The actual rate over a fund year that will be received by any individual will depend on the member's opening account balance and cash flow during the year.

2. Further, the allocations actually credited to a member's account often also include adjustments, such as transfers to and from reserves that are held by a fund, or are subject to deductions for non-investment based costs such as administration costs.

We expect that the intention of this requirement is to publish net investment returns which will allow the comparison of the investment performance of different superannuation funds. This can only be achieved if the net investment return published is the net investment return achieved on the assets that support the members' accounts – this is referred to as "net earnings" in Corporations Regulation 7.9.01.

We therefore suggest that the words, "of beneficiaries" be deleted from this sub-paragraph.

The Actuaries Institute would be pleased to discuss the issues raised in this submission or to respond to specific questions to assist the Treasury in the course of its work. Please do not hesitate to contact Andrew Boal, Convenor of the Superannuation Practice Committee on (03) 9655 5103 (andrew.boal@towerswatson.com) or Chief Executive, Melinda Howes, on (02) 9239 6106 (melinda.howes@actuaries.asn.au) if there is any way we can assist.

Yours sincerely

David Goodsall
President

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13 April 2012

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

Dear Mr Jones

INVESTMENT LEAGUE TABLES

The Actuaries Institute ("the Institute") is the sole professional body for actuaries in Australia, providing independent, expert and ethical comment on public policy issues where there is uncertainty of future financial outcomes. It represents the interests of over 3,800 members, including more than 2,000 actuaries.

Some of the principles that guide the Institute's inputs into public policy are:

- Acceptance of public sector involvement where the market does not meet societal needs,
- The need to take a long term policy view, with appropriate transitional arrangements,
- Ensuring that consequences of risk taking behaviour are borne by the risk taker,
- Issues of intergenerational equity, and
- Clear and reliable information available for decision-making.

Relevant to this letter, some of our members had significant involvement in the development and publication of Australia's first superannuation investment performance surveys. We note that APRA has indicated that it intends to publish Investment Performance data for individual superannuation funds. APRA has also indicated that it intends to provide a mechanism by which the performance of these funds will be ranked.

Overview

The Institute supports APRA providing a wide range of Investment Performance data relating to Australian superannuation funds. We believe that there are many experienced investment and superannuation specialists who will be able to analyse and interpret such data. This will enable the industry (and superannuation fund members) to better assess the investment skills of the various superannuation funds available in Australia.

We are, however, cautious about the format of any Investment Performance League Table that is produced by APRA.

When considering the structure of Investment Performance League Tables we must first establish the reasons why such tables are to be published. The Institute expects the primary purpose of such tables will be to assist members of superannuation funds and their advisers to make judgements about the investment capabilities of the various funds in the tables.

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We believe that these tables should therefore have the following characteristics:

1. The tables must set out investment returns that represent the outcomes generated by the investment activities of the funds in the survey.
2. The tables should cover a sufficiently long enough period to represent the longer term investment skills of the funds in the survey.
3. The tables should provide an insight into any trends in the investment returns over the period of the survey and, to the extent possible, should not suggest trends that do not exist.
4. The information set out in the tables should provide an indication of the relative performance of each of the funds in the tables.
5. The tables should provide an indication of the way that investment returns vary over time.
6. The tables should provide broad indicators that will help members to assess the overall performance of all funds and the relative performance of each of the funds over the period covered by the survey.
7. The tables should include an indication of the investment fees and other investment costs associated with investment returns of each fund investment option.

We recognise that assessing investment performance is not a straightforward task, and any set of tables will represent a practical compromise between simplicity and comprehensiveness. However, as far as possible, the tables should attempt to address all of the above requirements.

In the past, the most common form of Investment League Table has been one that sets out the annual compound rate of investment return net of all investment fees, costs and taxes calculated for periods of 1, 3, 5 and possibly 10 years. Importantly, these returns are all calculated for periods ending on the same end date, rather than independent periods ending on different dates. The Institute has reviewed this approach and considers that it may lead to members making poor choices.

Therefore, the Institute has developed an alternative approach in which the investment return for an investment option is to be reported for three contiguous four year periods. The disadvantages of the traditional approach, and the comparative advantages of the Institute's proposed alternative approach, are considered below.

1) Average Annual Compound Rate of Return

With the traditional approach the average annual compound rate of return for all of the three (or four) reported periods is affected by the return that a fund has achieved in the most recent years. This can indicate superior long-term investment performance that has not taken place.

An example is a balanced fund investment option for which a fund's recent superior performance can be purely the result of a one-off decision to lower its allocation to an asset class that has underperformed in the last year. If other funds have not taken the same position, the traditional reporting approach will indicate that this fund has superior long-term performance.

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However, our suggested approach will identify that the superior performance has only affected one period. Members will then need to establish the reason for this superior recent performance and determine whether it will continue in the future.

Another example is where an Investment option is invested entirely in Australian shares. The performance of "value" or "growth" stocks tends to outperform the overall market from time to time. This means that the relative performance of a particular Australian share investment option for a particular year may be simply the result of a bias to the outperforming sector of the share market rather than the result of superior investment capabilities.

If one fund's recent performance has been significantly better than other funds because of this bias, this outperformance will also influence the relative performance for longer periods using the traditional approach. This would suggest the fund has superior investment capabilities over the longer term, when all that has happened is that the fund has benefited from a bias to a market sector that happened to outperform the overall market in recent years.

Importantly, when this bias produces underperformance simply because another sector of the market has outperformed, the reverse is the case.
Our suggested approach will help to identify if a fund has been able to add value in each of the four year periods, for example by changing its exposure between value and growth stocks as performance of these sectors varies over time, as opposed to a bias to one style which may outperform from time to time.

2) Trends in Relative Performance

The reported returns can mask trends in relative performance over time and create apparent trends that do not actually exist.

As the periods investigated for the traditional approach all end on the same date, any trends in the relative performance of a fund over time are dampened by the fact that the average compound rate of returns for all longer periods include the return achieved in the most recent years of the period.

An important disadvantage of the traditional approach is that it may also create trends that do not exist. Consider, for example, a fund that has a significantly higher investment return than other funds in the most recent year, but only average returns in every other year. With the traditional approach, this fund will have superior returns (relative to other funds in the table) for all periods. Further, considering the relative returns for each of the periods will indicate a trend over the longer term of steadily improving relative performance. This is clearly not the case as the fund in question will have only outperformed other funds in one year.

Our suggested approach can assist members to determine how a fund's relative performance has changed over time and identify any trends in this relative performance over that time.

3) Volatility of Returns

With the traditional approach reported returns do not clearly show the inherent volatility of returns over shorter periods or that significant differences can occur between the returns achieved by funds over shorter periods.

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As the period used to calculate returns increases, the volatility of actual returns and relative returns reduces. This smoothing effect may be increased by the survivorship bias inherent in the fact that there is a tendency for funds with the worst relative performance to cease to operate. Therefore, the longer term results represent the performance of the better performing funds.

Our suggested approach will show the average of the absolute returns over three separate four year periods. Although four year periods will smooth out some of the volatility demonstrated by one year returns, we would expect that there will still be significant differences between the returns in each of the periods.

Additional Metrics

The Institute is also recommending that additional metrics be included in the Investment League Tables to help members assess the relative performance of the funds in the survey.

It has been common practice to rank each fund's investment performance for each of the periods. It is an indication of relative performance. However, it has the potential to mislead members who are less financially sophisticated because the number of funds with results tends to reduce as the period being considered increases.

For example, consider a fund that has median performance in each of, say, three periods where the number of funds with results for each of the periods was 100, 70 and 50 respectively. The ranking of this fund in each of these periods would be 50, 35 and 25 respectively. It would be clear to anyone who understands ranking that the fund's relative position had not changed. However, for the less sophisticated person there is the risk that the change in the number over the periods would be seen as a worsening of the fund's relative position.

To overcome this problem, the Institute recommends that the percentile of each fund is included in the Investment League Table as well as the fund's rank.

Our Suggested Approach

Having regard to these issues with the traditional approach to Investment League Tables, the Institute has developed an approach which we believe improves the effectiveness of the investment performance analysis and overcomes many of the problems associated with the traditional approach. We refer you to the proposed Investment League Table attached.

Some comments on our proposed approach are set out below.

1. The Investment League Table sets out the past investment performance for three separate four year periods and for the total twelve year period. The use of three four year periods addresses most of the issues discussed above with the traditional investment league tables.

    a) The performance of each period is reported separately. Therefore members can obtain an understanding of the investment performance from time to time without this being dominated by the most recent performance.

    b) Four-year periods have been selected as we believe that consecutive four-year periods should demonstrate the impact of any style bias in the portfolio of a particular fund and also the impact of medium term investment cycles.

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c) Trends in relative performance over the twelve year period are more evident and less dominated by the relative performance in the most recent period.

d) The volatility of actual and relative performance over the twelve year period is evident.

e) We note that the issue of survivor bias in the later periods is still an issue. We do, however, believe that, with our approach, the number of funds in each of the four year periods will be slightly more obvious to members.

2. We have included the rank of each fund for each four year period and for the entire twelve year period. We believe that members will understand the concept of a fund's rank and this will help them to more easily judge the relative performance of each fund for each period.

3. We have included the Percentile of each fund. We accept that many members will struggle to understand this concept. However, the Percentile of each fund has the advantage (when compared to a fund's rank) that it provides a measure of the relative performance of funds that is independent of the number of funds in the Investment League Table. The Percentile has the added advantage that Percentiles can be compared over different time periods. For example, if we consider a fund that has median performance in each of the four year periods, its Percentile in each of the periods will be 50%. Importantly, this analysis can be carried out by considering the actual level of the Percentile without actually fully understanding how the Percentile is calculated.

   We have highlighted the Percentile column as we believe that this is the most important information for a member to consider. This data provides a member with the relative position of each fund's investment performance, how the level of its investment performance compares with other funds for the period and how the fund's relative performance has changed over time.

   We have also included the median return for each period. We recognise that many members will not know what a median is. However, the inclusion of the median Percentile will provide members with a guide to its relevance. For those members who do know what a median is, this statistic provides a simple benchmark against which the absolute level of each fund's investment performance can be measured.

4. The Investment League table is based on the Net Investment Return achieved by each fund. The Net Investment Return is the Gross Investment Return less all investment fees, other investment costs and taxes. We note the following:

   a) We have based the league table on net investment returns. We believe that members will be interested in the investment return that underlies investment allocations or crediting rates added to their accounts. This will be determined by the combined effects of the gross investment return achieved, the investment fees and costs and the investment taxes that were incurred in achieving this return.

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b) Members might, or should, also be interested in fund reserving and allocation methodologies and allocation or crediting results achieved - these are important matters but we believe they should be examined separately.

c) We have assumed that only investment fees, other investment costs and taxes will be deducted from the gross investment return. We believe that the deduction of any other fees, costs or taxes would not result in a proper basis to compare the relative investment performance of funds.

5. We have included the expected level of the investment fees and other investment costs. Importantly, we believe that this should be the level of investment fees and costs stated in the fund's PDS rather than any measure of the past level of these fees and costs. As stated above, we believe that it is the net investment performance that should be examined when considering the investment capabilities of a fund. We do accept however, that members will want to know what level of fees and other investment costs they will be paying to achieve their investment return. We suggest that it is the fees and other investment costs that will be charged in the future that is important in this context.

6. We recommend that only 1 July to 30 June returns be included in the Investment League Table as the majority of funds have fund years that end on 30 June. This will mean that the investment returns for most funds will be based on exact information which has been audited. It is also important that the investment returns for all funds are calculated for exactly the same periods. Even small changes in the start and end dates of the periods used to calculate investment returns may result in significant differences in the level of the investment return. The start and end dates for the periods used must be the same for all funds to ensure that the comparison between funds is not misleading.

7. We accept that many funds will not have a full twelve years of experience. However, most major funds would have at least eight years of experience for an investment option that could reasonably be argued to represent the current investment option. Further, the fact that some funds only have four years of experience is important information for members as this will alert them to the age of the fund.

8. A new fund will not, by definition, have four years of experience. We believe that the performance of any new fund should not be included in a table that is to be used to compare the investment capabilities of funds. We accept however, that funds should be allowed to include past investment performance if it can be properly demonstrated that it is representative of the investment performance of that investment option.

There are other investment matters that should be considered by members and could be included in league tables – such as investment objectives, volatility, risk, liquidity and whether "active' or "passive" investment. We are currently exploring how best to collate and rank these and intend to make further recommendations. The enclosed copy of a recent article published in the December 2011 edition of *Actuary Australia* should give you some indication of what we have in mind.

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We recognise that some superannuation fund members may not fully understand the proposed League Tables. However it is important that any table does not lead superannuation fund members to incorrect conclusions about the investment capabilities of the various funds in the table. We believe, for the reasons outlined above, that our suggested approach has a lower likelihood of misleading the less financially sophisticated members of superannuation funds. Further, we would expect that, once the tables have been published, the popular press will explore them and provide in-depth analysis thereby helping superannuation fund members understand the implications of these tables.

We also recognise our suggested approach is significantly different to what has been generally used by the superannuation industry in the past. We therefore intend to consult with other groups who are actively involved in the superannuation industry to obtain their feedback (and input) on our proposal.

We would welcome the opportunity of meeting with an appropriate person or group to provide more details of our proposals. Please contact Melinda Howes, Chief Executive of the Actuaries Institute (Phone: (02) 9239 6106 or melinda.howes@actuaries.asn.au) if you would like to arrange this, or for any further information.

Yours sincerely,

David Goodsall
President

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Net Investment return

Fund	Last 4 years (1/7/07 to 30/6/11)			Previous 4 years (1/7/03 to 30/6/07)			First 4 years (1/7/99 to 30/6/03)			12 years (1/7/99 to 30/6/11)			Current Investment fees & costs
	Number of funds		103	Number of funds		71	Number of funds		57	Number of funds		57	
	Net Investment return pa	Rank	Percentile	Net Investment return pa	Rank	Percentile	Net Investment return pa	Rank	Percentile	Net Investment return pa	Rank	Percentile	
	(Note 1)	(Note 2)	(Note 3)	(Note 1)	(Note 2)	(Note 3)	(Note 1)	(Note 2)	(Note 3)	(Note 1)	(Note 2)	(Note 3)	
Fund A	3.7%	(6)	94%										0.45%
Fund A1	4.0%	(3)	97%	9.3%	(32)	55%							0.56%
Fund A2	-0.4%	(91)	12%	10.1%	(11)	85%	3.0%	(31)	46%	4.2%	(33)	42%	0.37%
Fund A3	4.0%	(3)	97%	6.3%	(64)	10%	1.7%	(47)	18%	4.0%	(40)	30%	0.62%
Fund B	1.4%	(52)	50%	10.5%	(2)	97%	4.4%	(15)	74%	5.4%	(12)	79%	0.37%
Fund B1	-1.3%	(97)	6%	8.7%	(41)	42%	1.0%	(51)	11%	2.7%	(50)	12%	0.22%
Fund B2	-1.3%	(97)	6%	8.7%	(41)	42%	1.0%	(51)	11%	2.7%	(50)	12%	0.63%
Fund B3	-0.2%	(90)	13%	7.9%	(54)	24%							0.22%
Fund C	0.7%	(72)	30%	8.1%	(53)	25%	0.8%	(53)	7%	3.1%	(49)	14%	0.68%
Fund C1	1.8%	(42)	59%										0.23%
Fund C2	0.2%	(88)	15%										0.33%
Fund C3	3.5%	(8)	92%										0.43%
Fund D	2.6%	(26)	75%	6.8%	(61)	14%	1.7%	(48)	16%	3.7%	(43)	25%	0.51%
Fund D1	3.2%	(11)	89%	8.6%	(46)	35%	3.2%	(27)	53%	5.0%	(22)	61%	0.62%
Fund D2	1.2%	(60)	42%	8.5%	(48)	32%							0.27%
Fund D3	0.5%	(76)	26%	5.5%	(66)	7%	6.3%	(4)	93%	4.1%	(37)	35%	0.45%
Fund E	1.6%	(50)	51%	8.2%	(51)	28%	6.7%	(3)	95%	5.4%	(11)	81%	0.61%
Fund E1	0.9%	(67)	35%										0.21%
Fund E2	2.9%	(16)	84%										0.31%
Fund E3	1.7%	(45)	56%	10.5%	(3)	96%	4.9%	(10)	82%	5.7%	(6)	89%	0.51%
Fund F	1.9%	(37)	64%	9.3%	(34)	52%							0.55%
Fund F1	0.3%	(86)	17%	5.8%	(65)	8%	0.7%	(54)	5%	2.2%	(55)	4%	0.25%
Fund F2	0.3%	(84)	18%	5.3%	(67)	6%							0.56%
Fund F3	1.8%	(43)	58%	9.6%	(22)	69%							0.27%
Fund G	1.7%	(47)	54%										0.38%
Fund G1	0.4%	(80)	22%										0.54%
Fund G2	1.2%	(57)	45%										0.46%
Fund G3	1.6%	(51)	50%	10.3%	(8)	89%	5.2%	(9)	84%	5.6%	(8)	86%	0.61%
Fund H	2.8%	(19)	82%	9.7%	(20)	72%	6.3%	(5)	91%	6.2%	(2)	96%	0.51%
Fund H1	2.8%	(19)	82%										0.22%
Fund H2	2.9%	(15)	85%	10.4%	(5)	93%	3.3%	(26)	54%	5.5%	(10)	82%	0.39%
Fund H3	1.3%	(55)	47%	10.4%	(6)	92%	4.4%	(14)	75%	5.3%	(14)	75%	0.32%
Fund I	4.4%	(1)	99%										0.31%
Fund I1	0.4%	(82)	20%	7.6%	(55)	23%	2.2%	(44)	23%	3.4%	(47)	18%	0.64%
Fund I2	0.6%	(75)	27%	8.7%	(40)	44%							0.32%
Fund I3	2.7%	(24)	77%	9.8%	(19)	73%	2.9%	(32)	44%	5.1%	(19)	67%	0.34%
Fund J	1.8%	(43)	58%	5.1%	(68)	4%	0.1%	(56)	2%	2.3%	(54)	5%	0.59%
Fund J1	0.5%	(79)	23%	8.1%	(52)	27%	2.4%	(40)	30%	3.6%	(44)	23%	0.36%
Fund J2	1.0%	(65)	37%										0.54%
Fund J3	0.4%	(81)	21%										0.58%
Fund K	0.7%	(69)	33%										0.35%
Fund K1	1.2%	(56)	46%	9.4%	(27)	62%	3.1%	(30)	47%	4.5%	(27)	53%	0.70%
Fund K2	3.2%	(12)	88%	8.6%	(45)	37%	6.0%	(6)	89%	5.9%	(3)	95%	0.54%
Fund K3	2.6%	(27)	74%	9.6%	(21)	70%	3.4%	(24)	58%	5.1%	(18)	68%	0.58%
Fund L	2.1%	(32)	69%	8.4%	(50)	30%	3.2%	(28)	51%	4.5%	(26)	54%	0.36%
Fund L1	2.5%	(29)	72%										0.57%
Fund L2	2.5%	(28)	73%										0.51%
Fund L3	2.8%	(18)	83%	10.0%	(13)	82%							0.68%
Fund M	2.0%	(36)	65%	9.5%	(25)	65%	5.5%	(8)	86%	5.6%	(7)	88%	0.32%
Fund M1	0.1%	(89)	14%	9.5%	(24)	66%	1.2%	(50)	12%	3.5%	(45)	21%	0.28%
Fund M2	1.1%	(61)	41%	10.4%	(7)	90%	5.7%	(7)	88%	5.7%	(5)	91%	0.37%
Fund M3	1.1%	(61)	41%										0.65%
Fund N	1.0%	(63)	39%	10.1%	(9)	87%	4.2%	(16)	72%	5.0%	(20)	65%	0.49%
Fund N1	1.0%	(63)	39%	10.1%	(9)	87%	4.2%	(16)	72%	5.0%	(20)	65%	0.60%
Fund N2	0.9%	(67)	35%	8.9%	(39)	45%	2.7%	(37)	35%	4.1%	(36)	37%	0.67%
Fund N3	1.6%	(49)	52%	9.8%	(18)	75%	1.6%	(49)	14%	4.3%	(31)	46%	0.29%
Fund O	0.2%	(87)	16%										0.45%
Fund O1	-1.2%	(96)	7%										0.63%
Fund O2	2.7%	(23)	78%	10.0%	(12)	83%							0.35%
Fund O3	0.7%	(72)	30%	9.6%	(23)	68%	3.3%	(25)	56%	4.4%	(28)	51%	0.68%
Fund P	3.1%	(14)	86%										0.27%
Fund P1	0.6%	(74)	28%										0.67%
Fund P2	-1.1%	(94)	9%	9.8%	(16)	77%							0.63%
Fund P3	-1.1%	(94)	9%	9.8%	(16)	77%	3.6%	(21)	63%	4.0%	(38)	33%	0.42%
Fund Q	1.3%	(54)	48%	8.7%	(43)	39%	2.7%	(38)	33%	4.2%	(32)	44%	0.69%
Fund Q1	0.9%	(66)	36%	8.6%	(44)	38%	2.9%	(33)	42%	4.1%	(35)	39%	0.68%
Fund Q2	-1.9%	(99)	4%	10.0%	(14)	80%							0.44%
Fund Q3	-0.9%	(93)	10%	7.6%	(56)	21%	0.5%	(55)	4%	2.3%	(53)	7%	0.70%
Fund R	-6.3%	(103)	0%	12.6%	(1)	99%	7.0%	(1)	98%	4.1%	(34)	40%	0.32%
Fund R1	2.9%	(16)	84%	9.4%	(28)	61%	3.9%	(19)	67%	5.4%	(13)	77%	0.47%
Fund R2	-2.8%	(101)	2%	3.9%	(71)	0%	0.0%	(57)	0%	0.3%	(57)	0%	0.37%
Fund R3	0.7%	(70)	32%	7.2%	(58)	18%							0.31%
Fund S	0.4%	(82)	20%	6.9%	(60)	15%	2.4%	(39)	32%	3.2%	(48)	16%	0.43%
Fund S1	1.2%	(58)	44%										0.61%
Fund S2	4.1%	(2)	98%	9.9%	(15)	79%	3.1%	(29)	49%	5.7%	(4)	93%	0.24%
Fund S3	1.6%	(48)	53%	6.4%	(63)	11%	2.3%	(42)	26%	3.4%	(46)	19%	0.30%

Net Investment return

Fund	Last 4 years (1/7/07 to 30/6/11) Number of funds 103			Previous 4 years (1/7/03 to 30/6/07) Number of funds 71			First 4 years (1/7/99 to 30/6/03) Number of funds 57			12 years (1/7/99 to 30/6/11) Number of funds 57			Current Investment fees & costs
	Net Investment return pa (Note 1)	Rank (Note 2)	Percentile (Note 3)	Net Investment return pa (Note 1)	Rank (Note 2)	Percentile (Note 3)	Net Investment return pa (Note 1)	Rank (Note 2)	Percentile (Note 3)	Net Investment return pa (Note 1)	Rank (Note 2)	Percentile (Note 3)	
Fund T	1.8%	(40)	61%										0.30%
Fund T1	2.1%	(34)	67%	8.9%	(38)	46%	2.3%	(43)	25%	4.4%	(30)	47%	0.69%
Fund T2	2.6%	(25)	76%	9.3%	(35)	51%	2.8%	(35)	39%	4.8%	(23)	60%	0.61%
Fund T3	2.1%	(33)	68%										0.52%
Fund U	1.7%	(46)	55%										0.20%
Fund U1	2.1%	(31)	70%	6.8%	(62)	13%	2.8%	(34)	40%	3.9%	(42)	26%	0.68%
Fund U2	4.0%	(3)	97%	9.3%	(32)	55%	6.9%	(2)	96%	6.7%	(1)	98%	0.37%
Fund U3	2.1%	(30)	71%										0.46%
Fund V	1.8%	(41)	60%	7.4%	(57)	20%							0.45%
Fund V1	1.2%	(59)	43%										0.59%
Fund V2	0.7%	(70)	32%	5.0%	(69)	3%	1.7%	(46)	19%	2.5%	(52)	9%	0.36%
Fund V3	3.4%	(9)	91%										0.63%
Fund W	-4.3%	(102)	1%	9.1%	(37)	48%	2.1%	(45)	21%	2.2%	(56)	2%	0.67%
Fund W1	1.9%	(37)	64%	9.4%	(30)	58%	4.4%	(12)	79%	5.2%	(16)	72%	0.64%
Fund W2	1.9%	(37)	64%	9.4%	(30)	58%	4.4%	(12)	79%	5.2%	(16)	72%	0.27%
Fund W3	3.2%	(10)	90%	8.4%	(49)	31%	2.7%	(36)	37%	4.8%	(24)	58%	0.27%
Fund X	3.1%	(13)	87%	9.4%	(26)	63%	4.1%	(18)	68%	5.5%	(9)	84%	0.48%
Fund X1	0.5%	(77)	25%	4.7%	(70)	1%							0.62%
Fund X2	1.3%	(53)	49%	8.5%	(47)	34%	2.4%	(41)	28%	4.0%	(39)	32%	0.26%
Fund X3	2.7%	(22)	79%	9.2%	(36)	49%	3.9%	(20)	65%	5.2%	(15)	74%	0.31%
Fund Y	0.3%	(85)	17%										0.31%
Fund Y1	2.0%	(35)	66%										0.40%
Fund Y2	0.5%	(78)	24%	9.4%	(29)	59%	3.5%	(22)	61%	4.4%	(29)	49%	0.68%
Fund Y3	2.8%	(21)	80%										0.55%
Fund Z	-0.5%	(92)	11%										0.56%
Fund Z1	-2.7%	(100)	3%	10.4%	(4)	94%	4.5%	(11)	81%	3.9%	(41)	28%	0.30%
Fund Z2	3.7%	(7)	93%	7.0%	(59)	17%	3.5%	(23)	60%	4.7%	(25)	56%	0.22%
Median	**1.4%**		**50%**	**9.2%**		**50%**	**3.1%**		**50%**	**4.4%**		**50%**	**0.45%**

Note 1 " Net Investment Return pa" for a fund is the average compound rate of investment earnings for the period after deducting all investment fees, costs and taxes.

Note 2 "Rank"for a fund is the relative position of the fund's net investment return for each period compared to the rates for all the 57, 71 or 103 funds in that period. The fund with a Rank of 1 has the highest net investment return.

Note 3 "Percentile" for a fund is the percentage of funds in the period that have a net investment return that is lower than the return of that fund. If 100 funds have investment returns for the period, and 60 funds have a lower net investment return than a particular fund, then the Percentile of that fund is 60%.

Superannuation for Dummies

Lack of investor engagement with superannuation is a widespread issue. The Institute Benefits Projection Working Group provides guidance on fee comparison for retail investors, and argues standardised measures would help both consumers and financial advisers.

A major finding from the Government's Cooper Review into the superannuation system was that it is too complicated, and as a result, people are not engaging with their superannuation.

Superannuation is a complex product. It packages insurance, investment and retirement funding – each of these can be a difficult technical topic in itself. Thus, it is not unusual that consumers' eyes glaze over when confronted by the jargon used in modern superannuation literature.

However, even granting the inherent complexity of superannuation, the current regulatory structure does very little to help interested consumers understand and compare superannuation products.

Investors would be better equipped to make decisions about super if the Government mandated standardised measures and terminology for more meaningful comparison of investment strategies and fees charged by superannuation funds.

Investment strategies – not just performance measures

When investors compare super funds, they should consider:

- the expected future return;
- the expected future volatility;
- their personal risk appetite; and
- other risk characteristics such as liquidity and risk of default.

One of the components of the Government's new 'Stronger Super' reform package is the introduction of a standardised 'MySuper' product as the basis for compulsory super contributions for employees who do not wish to choose their own investment strategy.

MySuper may go some way towards simplifying the investment component of superannuation, but employees will still need a method to compare MySuper strategies offered by different funds when they change jobs. The only tools currently at their disposal are the published past performance and the trustee's stated strategy and objectives. The major difficulties with these tools are a lack of standardisation in the calculation methods and the presentation of the results (if you can find them).

To help investors make informed comparisons and decisions about their super fund, the Government should mandate and provide free access to additional measures to facilitate more accurate comparisons of a fund's investment strategy:

- average performance, net of investment-related taxes, fees and costs, calculated on a consistent basis over one or more (agreed) timeframes;
- a measure of historical volatility, such as the 'standard risk measure';
- a liquidity measure such as the percentage of 'listed' versus 'unlisted' assets;
- a standardised investment expense ratio based on only investment-related fees and costs; and

- other standardised indicators of investment strategy differences such as 'growth' versus 'defensive' assets, overseas versus domestic assets, hedging ratio for overseas assets and use of 'active' versus 'passive' management.

Many fund members would need professional advice to understand and apply all of these measures, but they would be assisted greatly if advisers and commentators have access to a standardised set of regular performance measures.

Separating fees and costs

A major weakness of the current disclosure regime is a lack of clarity in how fees and costs are charged and disclosed. While fees are by no means the main driver of retirement outcomes, it should be possible for consumers to at least understand and compare the fees charged by different funds.

Some fees simply cover administration services such as the cost of collecting contributions, keeping records, and in some cases, additional services including web access and helplines. For most consumers, there's little point in paying extra fees for administration, unless they believe the additional services are worth the cost.

By contrast, many investors will be prepared to pay higher investment fees to gain access to asset classes that may earn better investment returns or achieve a better diversification.

The fees consumers are willing to pay should vary according to their life stage. For example:

- for younger employees starting their first job or changing employers for the first time, the focus will usually be on portability, simplicity and low fees;
- as employees move into the early stages of family life, when families are young and mortgages are high, a fund that provides optimum insurance may be the best solution; and
- later in their working life, when superannuation balances are larger, personal commitments are lower and retirement is much closer, employees may be more willing to pay a higher fee for professional advice regarding investment or retirement strategies.

To enable consumers to make informed super fund choices, fees and costs should be separated into three components:

1. **administration;**
2. **advice; and**
3. **investment.**

This may seem obvious, but many funds currently charge a single fee to cover all these components. Some funds charge a separate dollar fee for administration, but part of the "management fee" covers administration and advice, as well as investment management costs.

So what's the big deal? A young employee wanting to choose a low-cost fund to receive contributions from a part-time employer would have to understand the complexities of such a fund's investment strategy to be able to assess whether the package as a whole represents reasonable value for money – an unreasonable demand.

A major weakness of the current disclosure regime is a lack of clarity in how fees and costs are charged and disclosed. It should be possible for consumers to at least understand and compare the fees charged by different funds.

Comparing fees and costs

The Cooper Review suggested that the regulatory body (APRA) should produce a 'league table' enabling fund members to compare fees on a consistent basis.

The difficulty with this proposal is that the impact of administration fees on a fund member's account balance depends on the combination of fixed dollar and asset-based fees, and the size of the member's account balance and annual contributions.

As such, every case is different. Moreover, the fixation on fees is unhealthy, unless it is placed in the context of retirement outcomes (which are, after all, the ultimate objective of retirement funding policy).

A better approach would be to focus on the impact of administration fees and costs on the eventual retirement benefit outcome over a working lifetime. APRA could provide projections for a hypothetical employee starting a career at age 25 and retiring at age 65, ignoring differences in investment strategy, but showing the impact of administration fees and costs alone.

An even better approach would be for APRA to provide a standardised framework for super funds to do the calculations themselves. ▲

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1 August 2012

Default Superannuation Funds in Modern Awards
Productivity Commission
Locked Bag 2, Collins Street East
Melbourne vic. 800311111

By Email: default.super@pc.gov.au

Dear Sir/Madam

Response to Default Superannuation Funds in Modern Awards Draft Report

The Actuaries Institute is the sole professional body for actuaries in Australia. It represents the interests of over 3,800 members, including more than 2,000 actuaries.

On 13 April 2012, the Institute wrote to the Productivity Commission in relation to the Default Superannuation Funds in Modern Awards Issues Paper. We wish to take this opportunity to make some additional comments on one of the issues raised in the June 2012 Draft Report.

Management Expense Ratio

Section 4.3 of the Draft Report refers to the use of a "management expense ratio (MER)" to compare the costs of superannuation funds. The MER expresses the investment and operating expenses of a fund as a percentage of the fund's net asset value.

We note that the Commission has identified deficiencies with the MER which the Draft Report expresses as follows:

"The MER may not allow a uniform comparison across all funds (Finch 2005), and it will underestimate operating and investment expenses where embedded fees are incurred."

The Institute agrees and also considers that there are a number of other deficiencies with the MER which makes it unsuitable to use in comparing fund costs, including:

1. The MER mixes investment and administration costs. We have previously submitted to Treasury, APRA and ASIC that these costs must be considered separately for a valid comparison. The extent and effectiveness of the investment and operational (or 'administration") services and the associated fees and costs should be considered separately to ensure that a meaningful comparison is achieved. We attach as Appendix A (3 pages), an extract from our submission to the Cooper Review, which summarises the reasons for this conclusion.
2. If the MER approach is used to compare (only) administration costs, expressing these costs as a percentage of the value of fund assets is still unsound. Expressing administration costs as dollars per member would be an improvement because most direct administration fees are currently expressed this way, and a significant part of ongoing administration expenses varies with changes in membership numbers.

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3. The Commission makes it clear that the assessment of a fund should be from the perspective of what is in the best interests of the members. Therefore, the administration costs should only include costs which impact on members' benefits. Hence if an employer is paying all or some of the administration costs then the costs payable by the employer should not be included in the calculation. From an employer perspective, it is appropriate to consider all administration expenses.

To illustrate point 2 above, consider this simplified example.

Assume two funds have an administration fee of $1.50 per member per week and no other administration costs which directly or indirectly impact on members' benefits. Unless there is a difference in service levels, administration costs should not affect the choice between these two funds.

The following table shows how the ratio of administration costs to assets might vary in a particular year for members with different past membership periods.

Past Membership	Average Account Balance ($)	Administration Fee Charged ($)	MER(%)
1 year	2,250	78	3.47
2 years	6,863	78	1.14
3 years	11,706	78	0.67
4 years	16,791	78	0.46
5 years	22,130	78	0.35
6 years	27,737	78	0.28
7 years	33,624	78	0.23
8 years	39,805	78	0.20
9 years	46,295	78	0.17
10 years	53,110	78	0.15

Assume one fund has 20% of members with one year of membership, 60% with 5 years and 20% with 10 years, its MER would be 0.32. Assume the other fund has 30% of members with one year of membership and 70% with 5 years, its MER would be 0.48.

The MER approach suggests that the first fund has lower administration costs even though the funds' administration fees charged to individual members are identical. If dollar cost per member was used instead, this would give the correct conclusion (in these circumstances).

Section 4.3 of the Draft Report points out that: "The average MER of default superannuation funds has consistently trended below that of all superannuation funds (figure 4.2)". The above example demonstrates that this may not be due to lower administration costs. It may merely indicate that default funds, whose members would probably have greater periods of past membership, have higher account balances than non-default funds and hence lower MERs. Whether or not this is actually the case would of course require deeper analysis.

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The comparison of administration expenses and their impact on members on a sound basis is not easy. The Institute has previously submitted an alternative approach to various enquiries, including the Cooper Review. This alternative approach uses projections prepared by funds on a specified basis illustrating the effect on benefits for say 5 membership periods, which would be included in Product Disclosure Statements. We attach, in Appendix B (5 pages), a further extract from our submission to the Cooper Review which explains this approach. We also attach, in Appendix C (4 pages), a letter we sent to APRA on 13 December 2011 about the form in which useful statistics on administration fee and costs could be collected and published.

Our Recommendation

Having regard to our comments above we recommend the following:

1. Only fees and costs that impact on members' benefits should be considered.
2. The MER approach discussed in the Productivity Commission's Draft Report should not be used in the assessment of fees and costs.
3. The fees and costs associated with investments and the fund's operation should be considered separately.
4. Draft Recommendation 4.3 should be reworded as follows:

"The selection and ongoing assessment of superannuation funds for listing as default funds in modern awards should include consideration of the following:

- The appropriateness of the investment fees and costs charged by the MySuper product, given its stated investment return objective and risk profile; and
- The appropriateness of the operating fees and costs charged to members by the MySuper product given the services provided and the quality and timeliness of those services."

Please contact either Melinda Howes, Chief Executive of the Actuaries Institute (phone (02) 9239 6106 or melinda.howes@actuaries.asn.au) or Andrew Boal, Convenor of the Actuaries Institute's Superannuation Practice Committee (phone (03) 9655 5103 or andrew.boal@towerswatson.com) if you would like to discuss our comments, or for any further information.

Yours faithfully

David Goodsall
President

Encls: Extract from Institute of Actuaries letter to Super System Review dated 18 November 2009
Standardised Disclosure of Fees and Costs - the Way Forward
Letter to APRA re Annual Statistics for MySuper Products dated 13 December 2011

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APPENDIX A

Extract from Letter to Super System Review dated 18 November 2009

REASONS FOR SEPARATING FEES AND COSTS

INTO INVESTMENT AND NON-INVESTMENT COMPONENTS

[*Five fruit or two apples and three oranges ?*]

The Institute's first recommendation is:

All superannuation fund expenses and superannuation fees and costs which impact on members' benefits should be subdivided into an "investment" component and an "administration" component for all purposes.

Without this it is not possible to give members and prospective members a sound basis for comparing the costs of two or more superannuation funds. To do this effectively, members need to know and consider:

(1) The fund administration fees and costs (and the services provided for those fees and costs), and

(2) The investment fees and costs (and the expected net investment returns) in respect of all the various investment options.

Administration fees and costs and investment fees and costs have different attributes which make it necessary to demonstrate their effect on members in different ways. This can only be done if the fees and costs are subdivided into administration and investment components. The most relevant attributes making subdivision essential are as follows:

ATTRIBUTES OF ADMINISTRATION FEES AND COSTS

1. Administration costs incurred by a fund are usually higher in the year the member is enrolled in the fund (marketing cost may also be significant) and in the year the member receives or commences to receive a benefit. In the intervening years servicing costs are lower and are often not expected to vary much from year to year. Funds seeking to allocate costs between members on an equitable basis reflect this pattern in the way fees and costs are deducted from member accounts. The costs to be met by a member should therefore be measured over the period of membership. As that period is not known in advance, figures for comparison between funds need to be provided for a number of membership periods - five periods are used in the recommended basis submitted.

2. Administration costs often vary according to the level of contribution (and/or the size of account balances) so that costs for more than one contribution level need to be provided for comparison of funds - two contribution levels are used, in the recommended basis submitted.

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3. In addition to the above variations in administration costs, the general level of a fund's administration fees and costs can vary from year to year e.g. in the year a major upgrade of the fund's computer administration system is necessary. For a fund operated by an institution the costs charged to members from year to year may be relatively stable as the institution may absorb the fluctuations over a period and make less frequent revisions to the fees payable to the institution by the fund. For a mutual fund, such as the typical industry or corporate fund, the fee may he relatively stable where administration is outsourced. The service provider may absorb the fluctuations over a period. However for a mutual fund handling all or most administration in-house, the costs can vary significantly from year to year. As the fees deducted from members' accounts in any year will differ from the actual costs in that year the difference is typically deducted from or added to investment income for that year. This is disclosed as a positive or negative "percentage of assets" administration fee or cost and may be averaged over say two or three years. (Other funds address this problem by putting administration fees deducted from member accounts into an account and paying administration expenses from that account. If the amount in the account is not sufficient, administration fees have to be increased. The current balance in the account may be disclosed in the PDS.)

ATTRIBUTES OF INVESTMENT FEES AND COSTS

1. Investment costs vary significantly (and reasonably) for different types of investment, typically being higher for growth investments such as shares and property. Accordingly costs must be disclosed separately for each investment option offered by the fund. For a master trust or similar offering a choice of investment manager as well as a choice of investment types, the number of options can be very large.

2. Investment costs for a particular investment type or option are not expected to vary much from year to year as a percentage of assets (except for performance fees). Accordingly it is usually sufficient to provide fees and costs for a single year for a valid comparison of funds.

Some have suggested it would be easier for members if the level of investment and administration fees and costs could be illustrated using one combined figure for the fund. This would be done by using only the investment cost for one investment option being that for a "balanced investment option". First this would not overcome the need for separate administration costs for different membership periods and different contribution levels. Secondly there is no such thing as a standard "balanced investment option". Some might include the same proportion of share investments but use different proportions of Australian and International shares. Some include infrastructure assets while others do not. Some might include a higher level of passive investments in the example used in the PDS and reduce or even exclude any active investments from the example. Some funds do not even have an investment option which could be regarded as a balanced investment option. Two funds could have the same basic fees and costs for their administration but the figures in the PDS could be very different because of the asset-mix used to calculate the cost for the "balanced option". While it would be simple to have just one figure it could be misleading and therefore may lead to the selection of a fund that does not best meet a person's requirements.

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Cost is not the only factor to be taken into account in selecting a fund. Different people want a different range of administration services. A person in stable employment and not close to retirement may only need basic administration services. A person who changes jobs frequently or is self employed or retired may have very different requirements. Likewise some want access to a wider range of product features (such as contribution, insurance, disablement and pension alternatives) and investment choices.

Having separate figures for administration and investment costs is not only more accurate for comparison purposes but makes it easier to select a fund providing the administration services required and the desired range of investment options.

The basis for disclosure submitted makes it easier for members and prospective members, not by compromising on the validity of the fund comparison but by using two simple tables, one for administration and one for investment. Also, where the administration element has more than one fee and cost component, the third step of the suggested disclosure regime avoids the need for the person to understand how each administration fee or cost component is calculated. It is the aggregate effect of these components as shown in the table which the person needs to know.

A beneficial consequence of the separation of fees and costs into "investment" and "administration" is that the unnecessary and confusing terms "management costs" and "other management costs", which are currently specified in Corporations Regulations, can be dispensed with.

Splitting the fees and costs is consistent with the definition of "net earnings" in Corporations Regulation 7.9.01. Also, in the United States new legislation was recently passed which requires 401k plans to separate their fees into administration and investment management components. Our recommendations are consistent with overseas developments.

We believe that separation of administration fees and costs from investment fees and costs is not difficult. Trustees will usually know the investment component of fees and costs, or can make a reasonable estimate. In practice, we believe that many trustees will already be regularly making a subdivision of these costs as part of normal internal supervision of the costs of operating the fund. Guidelines could be issued to clarify some details and achieve consistency.

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Standardised Disclosure of Fees and Costs - the Way Forward

[Updated November 2009]

The first version of this note was published in the August 2003 edition of *Actuary Australia*, the monthly magazine of the Institute of Actuaries of Australia. To take into account refinements suggested by various industry participants an updated version was published in the May 2004 edition of that magazine and another was included in our April 2007 submission to the Parliamentary Joint Committee on Corporations and Financial Services. For this November 2009 update we have incorporated some changes resulting from the work of the Institute of Actuaries Benefit Projections Working Group (of which Colin Grenfell and Ray Stevens are members) for its submissions to ASIC on benefit projections.

To help consumers compare different superannuation plans and products requires some standardisation in the way that fees, charges and costs are disclosed in Product Disclosure Statements (or PDS's). In fact, the same can be said of any product with an investment component, such as a managed fund or a life office or friendly society investment-linked policy or bond.

Just over ten years ago, Colin Grenfell wrote an article "KFS Disclosure - no easy matter" which was published by the Association of Superannuation Funds of Australia (ASFA) in the December 1998/January 1999 edition of SuperFunds. The article summarised the then public views on fee disclosure as expressed by the Liberal-National Coalition, the Labor Party, the Australian Securities and Investments Commission (ASIC), the Industry Funds Forum and others.

The article also noted that the Institute of Actuaries of Australia recommended that:

(1) Investment performance should be reported net of tax and investment transaction costs and net of all investment costs.

(2) Key Features Statements should include a brief description of all fees and charges.

(3) In addition there should be some form of analysis of the impact of fees and charges which should focus on all non-investment fees and charges.

(4) The impact of these fees and charges should be shown net of employer subsidies but should include any costs in excess of fees and charges which impact on members' benefits.

The authors of this note believe that these four recommendations reflect sound principles that remain valid today.

The authors note that the Institute's principles include the need to show separately the effect of investment fees and costs and of non-investment (or broadly administration) fees and costs. The authors consider this split is essential for a sound comparison of funds. The split also facilitates member investment choices. It is noted that the Report commissioned by ASIC from Professor Ian Ramsay, released in September 2002, recommended that investment and administration fees should be separated. Investment fees and costs would be defined consistent with Corporations Regulation 7.9.01 which refers to "… relating to the management of investment of fund assets".

In our previous work we have referred to non-investment fees and costs as “administration” fees and costs. The early material issued by the Cooper Review seems to have expressed a preference to call these non-investment fees and costs “superannuation” fees and costs rather than “administration” fees and costs. This is an innovative and very appropriate proposal which we support provided the new terminology is mandatory and clearly specified in regulatory guidance and/or legislation. We have therefore amended the terminology in this update to allow for this preference.

The August 2003 and May 2004 articles explain the background and relevant events since 1998. A further article in August 2005 expands on recommendations (1) and (3) above.

What happens next?

We suggest that the way forward should include the following three level fee and cost disclosure framework:

1. At a glance

This component of the framework would summarise the existence of various fees and costs using standardised terminology, order of contents and grouping. For example;

INVESTMENT		**SUPERANNUATION**	
Ongoing fees	***Yes***	Initial fees	***No***
Ongoing extra costs	***Yes***	Ongoing fees	***Yes***
Switching fees	***Yes***	Ongoing extra costs	***Yes***
Buy-sell spread	***Yes***	Benefit fees	***Yes***
		Exit fees or penalties	***No***

OTHER		
	Any other fees or costs?	***No***
	Are any dollar fees indexed	***Yes***
	Are fee rates expected to increase in the next 5 years?	***No***
	Are some tax deductions withheld?	***No***

2. Brief description

This component would be similar to the brief descriptions of fees and charges used in Member Booklets and some PDS's, but there would be a few important constraints. For example;

- Must include brief descriptions of how each of the above "***Yes***" responses is calculated and charged.

- Must start a new paragraph for each fee or cost.

- Must be in the same order as the first component and use the same grouping.

- Must briefly describe the services provided.

- Must use standard terminology similar in style and depth to the requirements of Corporations Amendment Regulations 2005 (No. 1) but, primarily as a consequence of the separation of fees and costs into "investment" and "superannuation" components, without the unnecessary and confusing terms "management costs" and "other management costs".

3. Impact of fees and costs

This third and final component would replace the current Corporations Regulations "example of annual fees and costs". Like the current example it would exclude service fees. It would have two distinct parts, one for Investment fees and costs and one for Superannuation fees and costs. For example;

INVESTMENT

For each investment option, list:

(a) the ongoing net of tax fees and extra costs as a single annual dollar amount per $10,000 of average assets (eg. if fees were .44% net of tax and the only other investment costs were Consultant's fees of .09% net of tax, then list $53 per annum for this option), and

(b) the buy-sell spread (if any) and state whether this margin is paid to the fund manager or left in the fund for the benefit of other members.

SUPERANNUATION

A standardised superannuation fees and costs projection (similar to that now required in the United Kingdom) for at least two levels of contributions. This is probably the most important part of the framework.

This part includes the following five columns for initial annual contributions of $5,000 and $10,000 respectively:

(1)	At end of years	2, 5, 10, 20 and 40
(2)	Total paid in to date	3 or 4 significant figures
(3)	Account balance without fees and costs deducted	3 or 4 significant figures
(4)	Effect of fees and costs to date	2 or 3 significant figures
(5)	Account balance with fees and costs deducted [= (3) - (4)]	3 or 4 significant figures

The Institute of Actuaries of Australia's 6 November 2008 response to ASIC Consultation paper 101 suggested, in its answer to Question 4 in Section B5 (page 30 of the response), how the two contribution levels in 3. above should be determined from time-to-time. The Institute suggested that they should be based on the future SG rate (and any soft compulsion rate of member contributions) applied to say 75% and 150% of an average weekly earnings figure (annualized) with the resultant annual contributions rounded to the nearest $1,000 and $2,000 respectively. For example, if average weekly earnings were $1,300 and the SG rate were 9%, then:

- Lower standard contribution = $1,300 x 0.75 x 52 x 9% = $4,563 = $5,000
- Higher standard contribution = $1,300 x 1.50 x 52 x 9% = $9,126 = $10,000

Sample Product Disclosure Statements

Two sample Product Disclosure Statements, which reflect the principles that we consider should apply to fee and cost disclosure, have been prepared and can be supplied if required. One sample is for a hypothetical Retail superannuation fund and the other is for a hypothetical Industry plan named "ZIS". (They have not been updated to reflect legislative or taxation changes since 2004.)

The next page is an extract from the latter PDS to illustrate the third component of our recommended framework.

This extract has been updated to amend the terminology for non-investment fees and costs from "administration" fees and costs to "superannuation" fees and costs and to use initial contributions of $5,000 and $10,000 as determined above.

We consider that if our proposal is adopted, the Australian Government Actuary should be given the responsibility of setting and monitoring the superannuation fee and cost projection basis.

We draw to your attention the following three important features of "Table 5":

- The first three columns would be common to all funds (when making a comparison of two or more funds, this feature gives the reader confidence that they are comparing "like with like").
- The fourth and fifth columns are unique to each fund since they depend directly on each fund's superannuation fees and costs.
- The fourth column shows that after 2 year's the effect of fees and costs (for ZIS) for a $10,000 initial annual contribution is **115%** of that for a $5,000 initial annual contribution but after 40 year's the effect of fees and costs for a $10,000 initial annual contribution is **191%** of that for a $5,000 initial annual contribution (this large relative difference demonstrates why with any comparator it is essential to have results for both short and long durations and for at least two contribution levels).

Colin Grenfell and Ray Stevens

[extract only]

Table 4: ZIS Annual INVESTMENT Fees and Costs Summary per $10,000 account balance in each investment option			
	Option A	Option B	Option C
Ongoing (and Extra)	$161	$140	$124
Buy-sell spread	Nil	Nil	Nil

Assumptions on which the following fee table is based

The table below uses the standard assumptions about account balance, contributions and investment returns that all funds must use to show the impact of their superannuation fees and costs. These assumptions are as follows:

- Account balance at start: nil.
- Initial Annual Employer contributions of $5,000 or $10,000 (before tax).
- Contributions payable mid-year (or say weekly) and increasing by 4.5% each year.
- Member contributions: nil.
- Net annual investment return of 7% (net of tax and net of investment fees and costs).
- Dollar fees increase by 3% each year.
- Results in **"today's dollars"** (ie deflated using a salary increase assumption of 4.5% each year) .
- No allowance for any tax payable on benefits.

Table 5: Effect of ZIS SUPERANNUATION Fees and Costs				
If withdrawn	**Total Paid in to date**	**Account Balance without fees and costs deducted**	**Effect of fees and costs to date ***	**Account Balance with fees and costs deducted ***
	Initial Annual Contribution $5,000			
after 2 years	$ 10,000	$ 8,700	$ 130	$ 8,570
after 5 years	$ 25,000	$ 22,560	$ 420	$ 22,140
after 10 years	$ 50,000	$ 47,940	$ 1,260	$ 46,680
after 20 years	$100,000	$108,700	$ 4,700	$104,000
after 40 years	$200,000	$283,000	$22,500	$260,500
	Initial Annual Contribution $10,000			
after 2 years	$ 20,000	$ 17,400	$ 150	$ 17,250
after 5 years	$ 50,000	$ 45,120	$ 610	$ 44,510
after 10 years	$100,000	$ 95,880	$ 2,080	$ 93,800
after 20 years	$200,000	$217,400	$ 8,500	$208,900
after 40 years	$400,000	$566,000	$43,000	$523,000

* The fees and costs include all fees and costs, except investment fees and costs and insurance charges. They include the benefit payment fee. For ZIS there are no other surrender penalties or exit fees and ZIS does not pay any commissions.

The last line of Table 5 (for an annual contribution of $10,000) shows that over a 40 year period the effect of the total deductions could amount to $43,000 (in today's dollars). Putting it another way, this would have the same effect as bringing investment returns down from 7% a year to 6.63% a year.

13 December 2011

Mr Ross Jones
Deputy Chairman
Australian Prudential Regulation Authority
400 George Street (Level 26)
SYDNEY NSW 2000

Dear Sir

APRA ANNUAL STATISTICS FOR MYSUPER PRODUCTS

The Actuaries Institute is the sole professional body for actuaries in Australia, providing independent, expert and ethical comment on public policy issues where there is uncertainty of future financial outcomes. It represents the interests of over 3,800 members, including more than 2,000 actuaries.

The Institute has made a number of submissions to the recent Super System Review and participated in other ways with the development of MySuper products.

We understand that APRA will be required to publish statistics relating to the fees and costs, and investment information, for MySuper and other superannuation products to facilitate comparisons by members. A Working Group of the Institute has done considerable work on these issues over recent years and has recently developed a discussion document on the form in which useful statistics on administration fees and costs of MySuper products could be collected and published.

The impact of administration fees and costs can be demonstrated in a number of ways. One approach is to calculate an "index" showing the projected benefit at the end of the membership period, expressed as a percentage of the projected benefit which would apply at the end of the membership period if there were no fees and costs affecting the member's benefit. Another is to show the "dollar reduction" in the projected end benefit (in today's dollars) caused by the administration fees and costs. We see merit in both these approaches.

Briefly, we believe that the main issues relating to reporting administration fees and costs to members are the effect of these fees and costs:

1. on members who have different contribution levels and different initial account balances, and
2. over different periods of membership.

We suggest that showing the impact of administration fees and costs given two contribution levels, say $5,000 p.a. and $10,000 p.a., and no initial account balance, would allow a member (or prospective member) of a fund to select the level which best matches the person's situation. We would not advocate showing the impact given a range of initial account balances, given the additional complexity that would be introduced.

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Comparisons over a 40 year membership period could be used for ranking funds, but a much shorter period, say 10 years, would highlight the fact that for some funds the effect of administration fees and costs can be different for shorter membership periods.

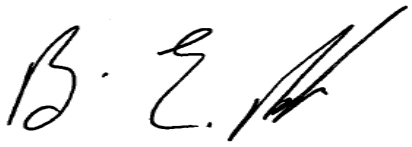
The attached document illustrates both the "index" and "dollar reduction" approaches described above, using $5,000 p.a. and $10,000 p.a. contribution levels. The impact of the administration fees and costs is shown over periods of 10 or 40 years for 27 Funds with administration fees and costs as described.

The Institute would welcome the opportunity to discuss with APRA the issues that we believe need to be considered. We propose to separately address the considerations in relation to investment statistics.

The calculations in the attached document are based on the principles that have been used in submissions relating to administration fees and costs in Product Disclosure Statements over a number of years by members of the Institute. We believe that consistency between APRA's data collection standards and ASIC's disclosure requirements is important.

We would welcome the opportunity of meeting with an appropriate person or group to provide more details of our proposal. Please do not hesitate to contact Melinda Howes, CEO on (02) 9239 6106 (melinda.howes@actuaries.asn.au) in this regard, or for any further information.

Yours sincerely



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ADMINISTRATION FEES AND COSTS

The two tables below provide information about the administration fees and costs charged by superannuation funds and the effect of these on members' benefits. Both of the tables exclude all fees and costs relating to investment. They also exclude insurance premiums and advice fees. The tables assume zero initial fund balances. If a member has an existing superannuation balance, then the tables do not indicate the full effect of administration fees and costs on the member's overall superannuation benefits.

Annual Contribution $5,000

If your annual contribution exceeds $7,500, see the blue table below

	Index (note 3) Membership		Effect of Fees and Costs (in today's dollars) Membership		Rank Membership	
	40 years (note 1)	10 years (note 2)	40 years (note 1)	10 years (note 2)	40 years (note 1)	10 years (note 2)
Fund 05	98.8	99.0	-$3,861	-$515	1	1
Fund 14	98.7	98.7	-$4,093	-$635	2	3
Fund 09	98.5	98.5	-$4,750	-$737	3	4
Fund 10	98.0	98.0	-$6,333	-$983	4	6
Fund 26	97.6	98.8	-$7,584	-$595	5	2
Fund 11	97.5	97.5	-$7,917	-$1,229	6	9
Fund 23	97.1	97.1	-$9,238	-$1,434	7	13
Fund 01	97.0	97.0	-$9,374	-$1,455	8	14
Fund 04	97.0	97.0	-$9,500	-$1,475	9	15
Fund 17	96.5	96.5	-$11,084	-$1,721	10	17
Fund 08	96.0	96.0	-$12,667	-$1,966	11	18
Fund 20	95.4	98.4	-$14,565	-$797	12	5
Fund 19	95.0	95.0	-$15,834	-$2,458	13	20
Fund 22	94.5	96.6	-$17,387	-$1,692	14	16
Fund 27	94.0	94.0	-$19,000	-$2,949	15	24
Fund 18	94.0	95.6	-$19,126	-$2,140	16	19
Fund 16	93.0	97.6	-$22,136	-$1,166	17	7
Fund 13	92.7	97.2	-$22,998	-$1,388	18	10
Fund 25	92.6	97.5	-$23,299	-$1,225	19	8
Fund 03	90.1	91.6	-$31,292	-$4,139	20	27
Fund 06	89.2	95.0	-$34,071	-$2,459	21	21
Fund 12	87.9	97.1	-$38,440	-$1,429	22	12
Fund 02	87.7	97.1	-$38,975	-$1,420	23	11
Fund 07	85.2	94.7	-$46,832	-$2,601	24	22
Fund 24	84.8	94.2	-$48,054	-$2,840	25	23
Fund 15	83.5	93.7	-$52,409	-$3,081	26	25
Fund 21	77.9	92.7	-$69,852	-$3,586	27	26

Please note:

1 This membership has been used to sort the above table (because 40 years is closer to the total potential membership of most people).

2 This membership has been included to illustrate how rankings may depend on the period of fund membership. Each fund's PDS shows the effect of fees and costs for periods of 2, 5, 10, 20 and 40 years.

3 The index provides a measure of how administation fees and costs effect members' benefits. The smaller the index the greater the effect on benefits. A fund where members incur no fees or costs (e.g. because they are paid by the employer) would have an index of 100.

	Annual Contribution $10,000					
	If your annual contribution is less than $7,500, see the green table above					
	Index (note 3)		Effect of Fees and Costs (in today's dollars)		Rank	
	Membership		Membership		Membership	
	40 years (note 1)	10 years (note 2)	40 years (note 1)	10 years (note 2)	40 years (note 1)	10 years (note 2)
Fund 14	99.4	99.4	-$4,093	-$635	1	2
Fund 05	99.3	99.5	-$4,561	-$539	2	1
Fund 09	99.3	99.3	-$4,750	-$737	3	3
Fund 10	99.0	99.0	-$6,333	-$983	4	5
Fund 11	98.8	98.8	-$7,917	-$1,229	5	6
Fund 23	98.5	98.5	-$9,238	-$1,434	6	8
Fund 04	98.5	98.5	-$9,500	-$1,475	7	9
Fund 17	98.3	98.3	-$11,084	-$1,721	8	10
Fund 26	98.0	99.2	-$12,451	-$763	9	4
Fund 08	98.0	98.0	-$12,667	-$1,966	10	12
Fund 01	97.5	97.5	-$15,707	-$2,438	11	16
Fund 19	97.5	97.5	-$15,834	-$2,458	12	17
Fund 27	97.0	97.0	-$19,000	-$2,949	13	20
Fund 22	95.8	97.8	-$26,885	-$2,133	14	14
Fund 20	95.6	98.5	-$28,090	-$1,428	15	7
Fund 18	94.8	96.5	-$32,873	-$3,430	16	21
Fund 03	94.0	95.6	-$37,769	-$4,363	17	23
Fund 16	93.5	98.1	-$41,256	-$1,840	18	11
Fund 13	93.5	97.9	-$41,467	-$2,038	19	13
Fund 25	92.9	97.8	-$44,829	-$2,161	20	15
Fund 06	89.3	95.1	-$67,630	-$4,833	21	24
Fund 12	87.9	97.1	-$76,651	-$2,819	22	18
Fund 02	87.7	97.1	-$77,950	-$2,839	23	19
Fund 24	86.1	95.6	-$88,113	-$4,302	24	22
Fund 07	85.4	95.0	-$92,170	-$4,945	25	25
Fund 15	83.5	93.8	-$104,411	-$6,091	26	27
Fund 21	78.9	93.9	-$133,355	-$5,999	27	26

Please note:

1 This membership has been used to sort the above table (because 40 years is closer to the total potential membership of most people).

2 This membership has been included to illustrate how rankings may depend on the period of fund membership. Each fund's PDS shows the effect of fees and costs for periods of 2, 5, 10, 20 and 40 years.

3 The index provides a measure of how administation fees and costs effect members' benefits. The smaller the index the greater the effect on benefits. A fund where members incur no fees or costs (e.g. because they are paid by the employer) would have an index of 100.