INSTITUTE OF PUBLIC ACCOUNTANTS®

Submission to the Senate Economics References Committee:

Inquiry into improving consumer experiences, choice, and outcomes in Australia's retirement system

February 2024

23 February 2024

The Chair
Senate Standing Committees on Economics
PO Box 6100
Parliament House
Canberra ACT 2600

Submitted via email: economics.sen@aph.gov.au

Dear Chair

Inquiry into improving consumer experiences, choice, and outcomes in Australia's retirement system

The Institute of Public Accountants (IPA) welcomes the opportunity to provide comments on the Inquiry into improving consumer experiences, choice and outcomes in Australia's retirement system.

Approximately three-quarters of IPA's members work in or advise the small business and small to medium enterprises sectors. Our submission is taken from this perspective.

Overall, consumer experiences, choice, and outcomes, would benefit from reducing complexity and providing reasonable and affordable product and service offerings to consumers. In any event, more qualified advisers need to enter the market to address the unmet financial advice needs of consumers. As the Assistant Treasurer the Hon Stephen Jones MP has often stated, there is a 'retirement crisis'. The role of qualified and regulated accountants should be considered against this environment.

Our summary and detailed responses are contained in the Attachment.

For any questions please contact Vicki Stylianou, Group Executive Advocacy and Professional Standards, Institute of Public Accountants at

Yours sincerely

[signed]

Vicki Stylianou
Group Executive, Advocacy & Professional Standards
Institute of Public Accountants

ATTACHMENT

Summary

The inquiry focuses on the retirement income system with terms of reference covering:

The regulatory and tax impediments for insurance products in retirement

- Complex and outdated pension rules in superannuation law are preventing product innovation.
- The intersection between pension rules, tax and social security law is preventing further take up.
- Trustees not having appropriate authorisations on their AFSLs, or adequate resources in their adviser/customer service personnel, to be able to give financial advice on such products.

The costs and opportunities of innovation in the retirement income system

- New pension products and capital protected products often require significant capital backing to develop and maintain, which not-for-profit trustees do not hold.
- Such products are highly regulated, and ASIC's current regulatory approach does not incentivise new product development (particularly the Design and Distribution Obligations (DDO) framework).
- Trustees will often partner with established providers (such as Challenger or Mercer) but can be reluctant to work with new entrants to the market on projects of any significance due to the regulatory scrutiny.

The potential role of FinTech in supporting retirement outcomes

- Digital advice might be utilised to help consumers navigate questions commonly asked about retirement products.
- Apps and other ready sources of information can provide fund members with access to information about their account balance and 'nudges' for further information when they might experience certain 'life events' like marriage, parenthood, retirement, etc.

Options to improve incentives and sustainability of the retirement income system, and progress in implementation of the Retirement Income Covenant.

- Reduce regulatory complexity in pension rules.
- Reduce friction between superannuation, tax, and social security legislation.

How can we support consumers to navigate retirement income?

- The transition from accumulation to retirement phase is so complicated that, ideally, everyone should receive personal financial advice. Having more information doesn't change the fact that, when trying to 'optimise' their retirement income, appropriately manage the risk that they may outlive their money, and retain enough capital to meet unforeseen risks, such as the significant lump sum and ongoing costs of aged care, retirees need to factor in many (changing) variables including: their superannuation balance, the pension they will be eligible for, their other assets, whether they have a spouse and dependants, the impact of their assets, and of the decisions they may make on social security entitlements, changing market conditions, unknown health care costs and aged care costs, their 'new' lifestyle in retirement etc. Even highly sophisticated individuals may not be able to navigate the transition themselves without professional help and they are likely to take a few years (after the transition occurs) to develop confidence in the decisions they make regarding the various aspects of their retirement.

- It is appropriate that the retirement income covenant, set out in section 52(8A) and section 52AA of the *Superannuation Industry (Supervision) Act 1993* (**SIS Act**), does not apply to SMSF members. Since members are themselves trustees; there is inherently an understanding of a member's needs in retirement. There is no requirement for data collection, or member segmentation etc. SMSFs are appropriately regulated by the Australian Taxation Office (**ATO**) and under the SIS Act.
- The 'take up of lifetime income products remains low, and the market remains undeveloped'. Even though the government has tried to incentivise 'innovative product design', there are still significant barriers to entry for trustees of superannuation funds seeking to develop such products themselves, or even to partner with dedicated retirement income product providers to bring a retirement income product offering to their members. Similarly, there are entry level barriers for advisers, who need to understand the complexity in the available products and develop their own comparative information to assist them to advise best fit in any particular situation. The current system simply does not allow for development of simple retirement products that will be supported by consumers and their advisers.

How are these issues being addressed by industry and other stakeholders to assist consumers?

- We are aware that the industry is grappling with the difficulty of providing educative or other general information in relation to the trade-offs faced by retirees in maximising their income in retirement, managing expected risks during their retirement, and enabling flexible access to funds, without triggering the full compliance obligations required by providing personal advice. For example, existing AFSL, disclosure, and privacy legislation impedes the ability of trustees and advisers to provide helpful information or general advice to retirees that spans the breadth of the issues that need to be considered. We consider the overly onerous personal advice requirements are partly responsible for the cost of personal advice and limited number of providers. The role of accountants (who have largely been unable to provide personal financial advice) should also be considered as part of the regulatory reforms needed to improve retirement outcomes going forward. Not having access to affordable advice options is a prime factor behind the low number of people seeking advice.
- In previous IPA submissions, including to ASIC (CP 332 Promoting access to affordable advice to consumers, January 2021), to Treasury on the ongoing consultations on the Quality of Advice reforms, the Review of the Tax Practitioners Board ('James review'), and various other consultations, the IPA has repeatedly recommended that the role of qualified accountants should be considered in addressing the unmet financial advice needs of Australian consumers, of which the financial adviser shortage is a major contributing factor.
- Further, the IPA was disappointed at the failure of the Quality of Advice review to adequately consider the role of accountants in financial advice (final report pp79-81). Despite acknowledging the problems with the limited AFSL, Michelle Levy missed the opportunity to make a significant contribution to addressing the adviser shortage, to the detriment of Australian consumers. We were bewildered as to how the report mischaracterised accountants and their work as 'most accountants are registered tax agents' (p79). The review also failed to adequately deal with Recommendation 7.2 of the Review of the Tax Practitioners Board which specifically recommended 'that the Government review the advice accountants can give in respect of superannuation'. This recommendation was referred to the Quality of Advice review for further consideration.

- We consider the current consultation to be a further opportunity to address the needs of Australian consumers by adding qualified accountants, who are highly regulated, to the broader pool of 'advisers'.
- The IPA would be pleased to provide further information on the role of accountants in providing superannuation (including SMSF) advice. Essentially, we support a consumer-centric model which would enable consumers to obtain advice on establishing and winding up SMSFs, contributions and a very limited number of topics, from suitably qualified accountants who have achieved further qualifications in the specific areas in which advice is to be given. The professional standing of accountants should be given recognition in the advice ecosystem.

What are the priorities and what are the risks in overcoming the issues?

- The removal of 'roadblocks in regulatory settings' is urgently required. At present, for example legislation applicable to licensing, disclosure and privacy may prevent a superannuation trustee from contacting a potential retiree, identifying longevity risk as a risk to be managed by a retiree, and suggesting that they consider a product designed to manage such a risk, such as a lifetime annuity issued by an insurance company. Similarly, professionals such as our member accountants, may be inhibited from providing helpful information, if they are not financial planners. Their ability to provide useful information should be valued appropriately, given the urgent need for retirees to be better informed. Many of the roadblocks have been long identified, and relevant solutions or improvements are known; in these instances, regulatory reforms could be fast tracked.
- Issuers of income stream products also need to be able to structure them, so that the retiree receives appropriate value from the product. Conventional annuities and pensions are typically seen as expensive, inflexible products, and these characteristics may be driven by the regulatory settings under which they are established. It seems to us that the Government could take a leading role in guaranteeing solvency, and offering long dated assets which an issuer of retirement income products could use to match their income stream liabilities.
- There is little information available to retirees, from Government or from financial firms which considers (or even alludes to) the inherent complexity of the retiree trade-offs[1], and the need to consider the breadth and depth of relevant factors. Even an up-to-date checklist on the MoneySmart site (or similar resource), with links to drill down on particular topics, would be helpful to retirees. A calculator tool, which allows the exploration of different scenarios, such as mapping the interaction of social security entitlements, the effect of buying a lifetime annuity, and the impact on super and income of such a purchase to assist decision making, would be very helpful.
- In order to induce the take up of retirement income products, retirees should not have their social security entitlements adversely affected when they apply capital available to take out a retirement income product.
- Some flexibility should be built into policy that allows members to exit a legacy product if a more suitable comparable product is available due to changes in legislation.

[1] Such as investing to boost expected income vs. limiting income risk, drawing income earlier vs. later, longevity protection vs. flexibility, paying for inflation hedging vs. higher expected income.

Other related matters

What does 'good' look like for how funds support and deliver products to their members in retirement?

- 'Good' would be simple, easy to understand, low on regulatory complexity, and with access to capital as well as income.

What basic information do members most need to assist their understanding and simplify decision-making about retirement income?

- That retirement phase, unlike accumulation phase, is not supported by default settings. Retirement requires retirees to understand their position and make certain decisions.
- Some information to help decision making about retirement income:
  - estimated life expectancy
  - income requirement
  - other assets eg property, savings
  - eligibility for age pension
  - spouse/partner (and their assets)
  - health care costs
  - aged care costs
  - where to get more help.
  - How the social security and/or a lifetime annuity may act as an 'insurance' against longevity risk, including indicative information about their availability and suitability (or when they will not be available or suitable).

Where can government and industry reduce complexity in the retirement income system, and provide simpler consumer experiences?

- The retirement income system is complex because each retiree has different circumstances: different income, time in the workforce, employment situation, capacity to save, home ownership status, superannuation balance, other assets, access to social security, risk preferences, financial literacy, partnership status and life events. The timeframe in retirement may be long, perhaps 30 or more years. And retirees' needs will change over that time as (for example) requirement for income is supplanted by the need to access aged care and medical care. Understanding the inherent complexity, and the ability to access suitable advice (not necessarily comprehensive advice, but rather timely advice relevant to a retiree's situation) is important. Changes to the advice rules that facilitate provision of timely relevant advice is important. We consider the overly onerous personal advice requirements are partly responsible for the cost of personal advice and limited number of providers. The role of accountants (who have largely been unable to provide personal financial advice) should also be considered as part of the regulatory reforms needed to improve retirement outcomes going forward. Not having access to affordable advice options is a prime factor behind the low number of people seeking advice. Refer above.
- We also consider that the interaction between social security, aged care and retirement income is difficult to navigate. Publicly available material, such as on websites, often does not address the interactions or the complexity.

How can funds utilise guidance, nudges, defaults etc to assist members into better solutions for their retirement income?

- Related considerations, relevant to regulatory barriers and provision of information, include when does too much communication from fund to member become problematic? What if members have opted out of receiving 'marketing' information?
- 'Nudges' inherently require trustees to consider personal information they hold about the member so they are tailored to the member's circumstances and therefore purposeful, which means they may comprise personal financial advice. 'Nudges' may also comprise recommendations that amounts to dealing by arranging. Each of these outcomes is a barrier to trustees and others providing more useful information to retirees. Independent financial advisers often provide this type of information to their advised clients but need to satisfy all the regulatory and compliance requirements, a significant cost for that business. Note too there is a conflict between obligations under the SIS Act and obligations under the Spam Act if a retiree has opted out of receiving marketing information.
- If communications only contain factual information, they may not be specific and clear enough to help members.

SMSFs – how do they manage risk, access assets and maximise their income; what about the application of the retirement income covenant?

- It is appropriate that the retirement income covenant, set out in section 52(8A) and section 52AA of the SIS Act, does not apply to SMSF members. Since members are themselves trustees; there is inherently an understanding of a member's needs in retirement. There is no requirement for data collection, or member segmentation etc. SMSFs are also adequately regulated by the ATO and under the SIS Act, and trustees and members often have the assistance of independent financial advisers. SMSFs will consider how they should meet a member's individual needs in the retirement phase, particularly in relation to the suitability of investments and access to capital, which must be considered as part of the existing investment covenant. Accordingly, SMSFs are appropriately regulated by the ATO and under the SIS Act.
- It would be useful if retirement income product providers such as life insurance companies were incentivised to provide better retirement products to SMSFs that are advantageous (or not disadvantageous) from a tax and social security law perspective and provide good value to retirees. Issuers of income stream products also need to be able to structure them, so that the retiree receives appropriate value from the product. Conventional annuities and pensions are typically seen as expensive, inflexible products, and these characteristics may be driven by the regulatory settings under which they are established. It seems to us that the Government could take a leading role in guaranteeing solvency, and offering long dated assets which an issuer of retirement income products could use to match their income stream liabilities.

What do funds need in order to deliver on better retirement income strategies?

- The removal of 'roadblocks in regulatory settings' is urgently required. Issuers of income stream products also need to be able to structure them, so that the retiree receives appropriate value from the product. Conventional annuities and pensions are typically seen as expensive, inflexible products, and these characteristics may be driven by the regulatory settings under which they are established. It seems to us that the Government could take a leading role in guaranteeing solvency, and offering long dated assets which an issuer of retirement income products could use to match their income stream liabilities.
- We need to be having more conversations about retirement, the kinds of decisions self-funded retirees need to make, and the fact that active engagement by retirees is necessary to achieve a

good outcome. Regulation should not inhibit the provision of more general information and general advice. Financial services are already heavily regulated, and we do not see the need for greater consumer protection at this time.

- Consumer protection is also less important for SMSFs – the trustees themselves are SMSF members and frequently are also advised. Further, SMSFs will consider how they should meet a member's individual needs in the retirement phase, particularly in relation to the suitability of investments and access to capital, which must be considered as part of the existing investment covenant.

What is the role of industry in supporting consumer protections and competitive products and services in retirement?

- The ability of industry groups such as our member accountants, to provide useful information should be valued appropriately, given the urgent need for retirees to be better informed.

What are the priorities and risks which should be considered in policy development?

- We consider the overly onerous personal advice requirements are partly responsible for the cost of personal advice and limited number of advice providers. The role of qualified accountants should be considered as part of the regulatory reforms needed to improve retirement outcomes going forward. Not having access to affordable advice options is a prime factor behind the low number of people seeking advice. Refer above.

How could lifetime income products be made more accessible?

- The lack of demand for lifetime income products seems to be due to behavioural biases. People would rather 'self-insure' against longevity risk by saving as much as possible, when a more rational approach would be to 'insure' their savings by purchasing an annuity and insure against unexpected health expenses by getting private health insurance. A comparison of the amount needed to be saved to provide the equivalent longevity risk to that provided by an annuity may assist to overcome these behavioural biases.
- Issuers of income stream products also need to be able to structure them, so that the retiree receives appropriate value from the product. Conventional annuities and pensions are typically seen as expensive, inflexible products, and these characteristics may be driven by the regulatory settings under which they are established. As mentioned above, government could take a leading role in guaranteeing solvency, and offering long dated assets which an issuer of retirement income products could use to match their income stream liabilities.

How is longevity risk managed and what could be done to improve it?

We consider the low take up of existing products to be indicative of their poor value and complexity, necessitated by regulatory requirements. Refer above.