2 March 2020

Senate Standing Committee on Economics
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Dear Committee Members,

This is a supplementary submission to our earlier submission dated 24 January 2020 on the Treasury Laws Amendment (Your Superannuation, Your Choice) Bill 2019. In it we provide further information to address questions, both technical and non-technical in nature, that we have been asked since our initial submission was made just over a month ago. UniSuper's main concern with the Bill remains the effect that it would have on our open Defined Benefit Division (DBD).

We strongly suggest that the Committee recommend that:

- The current exemption from the choice of fund requirements for *existing* defined benefit members should continue; and

- An exemption for those who are *newly* eligible to become defined benefit members should also be provided for in the legislation.

We believe it would be very beneficial for UniSuper's strong and valuable DBD to continue to provide excellent benefits for a large number of employees in the higher education sector whilst providing meaningful choice for those who wish such choice.

Under our preferred approach, new higher education employees who are eligible to become defined benefit members would continue to be automatically enrolled into UniSuper's DBD.

But they will have two key options. Firstly, they will have an option to elect to opt out of the DBD within 24 months, receiving into an accumulation account the same level of employer superannuation support as if they had remained a DBD member. And should they also wish to move to a different superannuation fund, they could opt to do so in the same manner that any non-defined benefit member would under this Bill. This could be thought of as a model of "deferred choice" and would ensure that we could continue offering our excellent defined benefit scheme to new members.

This submission provides some additional background on UniSuper, including our governance arrangements, our DBD and membership.

The Appendix to this submission provides significant amounts of statistics regarding the Fund and its membership.

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About UniSuper

UniSuper is Australia’s superannuation fund dedicated to people working in the higher education and research sector. With more than 450,000 members and over $85 billion in assets under management, we are one of Australia's largest super funds.

UniSuper is also one of Australia’s most awarded super funds, reflecting our ongoing commitment to deliver greater retirement outcomes for our members, by delivering high quality, value-for-money retirement saving products and services. We pride ourselves on being one of the best value service funds in the world, delivering strong short, medium and long term investment performance and excellent service, with very low fees.

For more than 35 years, UniSuper has worked alongside Australia’s universities and research institutes. We are extremely proud of the contribution the higher education sector makes in and to Australia.

Our origins

UniSuper, originally the Superannuation Scheme for Australian Universities (SSAU), was established in 1983 as a defined benefit (DB) scheme modelled broadly on then contemporary DB schemes in the Australian public sector and overseas peer funds. From its outset, the benefit design offered full portability of benefits across all participating employers and coverage of all permanent employees in the sector, including general, academic and professional staff.

The multi-employer and industrially-inclusive nature of SSAU led to some important distinguishing features from its commencement, in particular:

- a fixed contribution rate of 14% of salary p.a. for employers and 7% for members;
- by covering the whole university sector, members can maintain defined benefit membership when transferring between employers;
- members can defer their benefits (so maintain membership) through periods when not employed in the university sector;
- a formula-based benefit related to member’s salary, tenure and employment experience.

In 1998 an accumulation category was introduced as an alternative to defined benefit membership in SSAU. This is an accumulation-based benefit division, now known as Accumulation 2, based on the same 14% employer contribution rate.

Following the advent of award superannuation in the 1980s, a second fund, the Tertiary Education Superannuation Scheme (TESS) was established as an accumulation fund to accept the new 3% award (and later SG) contributions of employees who were not eligible to join SSAU, such as casual and short-term contract staff. The vast majority of existing and future SSAU members also became TESS members for this 3% award contribution to cover those employees in universities who were not eligible to join the SSAU. In 2000, the two entities were voluntarily merged into a single fund (UniSuper Limited) with a single Trustee Board, a single Consolidated Trust Deed and single administrator and management structure.

While we pre-date “award super” and “industry super”, we remain the result of a collective decision to offer a national scheme allowing for portability of benefits across the higher education sector.

Our ownership and governance

UniSuper Limited, the Trustee for the Fund, is owned by 37 university shareholders. Unlike the typical industry fund, there is no union ownership of UniSuper.

UniSuper’s Board comprises three independent directors, four employer representative directors and four member representatives, two of whom are appointed by unions (NTEU and CPSU). The Chairman’s position has always been filled by an independent director and UniSuper supplements the skills and professionalism of its Board by having two further independent directors. The three independent directors are all highly experienced investment and finance industry professionals having wide-ranging experience.

Our Board is very well respected for its strength and the alignment of our independent, university and union representatives.

UniSuper’s defined benefit division (DBD)

Almost all permanent employees in the higher education sector are enrolled in UniSuper’s open DBD upon joining the sector. As noted above, the standard employer contribution rate for DBD members is 17% of pay, 14% of pay going into the DBD pool and 3% of pay credited to each member’s additional accumulation account. In addition, DBD members also contribute an additional member contribution of 7% of pay (after tax), which they can reduce if they choose. As a result, the total standard contribution rate in respect of DBD members, of 21% of pay, significantly exceeds the Superannuation Guarantee rate.

DBD members do not have administration fees deducted from their accounts. The DBD benefit is quoted net of all costs and no administration fee is deducted from any associated accumulation balance held by the member. Consequently, the reasonable concern around duplicate accounts resulting in reduced retirement benefits due to multiple instances of administration fees being paid does not arise in respect of DBD membership.

We are keen to ensure that the choice legislation does not lead to detrimental impact for UniSuper members (including pensioners) or on the security of their retirement savings.

As at 30 June 2019, there were 84,615 active DBD members (contributors). There were also 5,087 deferred DBD members. The following table summarises the key statistics in respect of these members.

Number of active members	84,615
Average Salary	$109,400
Average age	44.8
Average Past Service	7.6 years
DBD Vested Benefits (active & deferred members)	$15.8 billion

In addition, there are over 10,000 pensioners receiving over $400m in annual defined benefit indexed pension benefits. The assets and liabilities of active DBD members and DBD pensioners are combined in one pool.

New members to the DBD and their options

Over each of the past 10 years, between 11,000 and 12,000 new members joined the DBD. Prior to 1998, the DBD was the only option for permanent employees; however, since then, new permanent employees who have defaulted into the DBD have had the option to switch to an accumulation product (Accumulation 2). The election to move to Accumulation 2 – the proportion of new DBD members electing to join Accumulation 2 – was about 10% in the mid-2000s, increased to about 20% in the mid-2010s but has since decreased to about 15%, as reported in the Fund's 1 July 2017 triennial actuarial investigation.

While all new permanent employees have a choice to opt out of the DBD during the election window, such new employees also have the ability to opt out of being a member of UniSuper altogether. Since 2006, universities have had rules in place that allow for up to 5% (10% at some universities) of those eligible for DBD membership to *not* join UniSuper. Employees who have opted out typically have been those wanting to remain in an existing superannuation fund, either accumulation or with defined benefits, such as the CSS or PSS or visiting academics from overseas. These rules were also established to prevent members having multiple superannuation accounts.

Existing defined benefit members beyond the 24-month election period

While the exemption from Choice for *existing* defined benefit members is being maintained, it is important to highlight that the removal of this exemption, which we don't expect, would introduce significant selection risks.

Allowing members to leave the defined benefit scheme without ceasing employment would enable some members to strategically "game" their exit. This likely would cause further instability to the funding of the DBD, especially during significant investment market volatility.

Ultimately, after the passing of the 24 month election period, a defined benefit member would remain in the scheme until they leave employment in the higher education sector. That is why we strongly support the statement below from paragraph 1.30 of the Explanatory Memorandum for this Bill:

> *The exemptions from providing choice to employees who are existing members of certain defined benefit schemes continue to apply.*

Therefore, as a result of the exemption in respect of existing defined benefit members, the key issue for us is how the choice measures would work for any employee who is not currently a defined benefit member but who becomes *newly eligible* to join a defined benefit scheme, such as ours.

It is not the *number* of new members that matters, it the *composition* of new members

A change in the total number of DBD members or the number of new DBD members or, even, a lack of new members would not concern us. What does concern us is a material potential increase selection risk. We do think that what is proposed in this Bill likely would introduce much higher risk.

Selection risk, particularly in relation to the salary growth profile of new members and the skewing of the average age of new DBD members, likely would increase if the DBD were not the default for the sector and if new members were able to opt in to the DBD. Under the proposed changes, our reading of this Bill suggests the intent would be for defined benefit eligibility to be, in effect, “opt in” to new employees. The Explanatory Memorandum supporting this Bill confirms this:

> *Existing employees who are not defined benefit members and who become newly eligible to join a defined benefit scheme do not need to be given a standard choice form unless requested (or another subsection of section 32N applies). New employees who are not existing defined benefit members but who are eligible to join a defined benefit scheme must be given a standard choice form within 28 days of commencing employment. Once an employee is a member of a defined benefit scheme the exemptions from the choice of fund requirements will apply where relevant.*
>
> (Paragraph 1.30 of the Explanatory Memorandum)

We are extremely concerned about the consequences of, and even the possibility of, a move to an “opt in” DBD. Selection risk would need to be much more closely monitored to ensure that the contributions in respect of future new DBD members are sufficient to cover the actuarial cost of their benefits. UniSuper has neither a Government guarantee or an employer guarantee to cover funding shortfalls. That is, employers are not obligated to make additional contributions should the total value of the DBD’s assets fall below its total liabilities. As a result, adverse outcomes from changes to experience ultimately would be borne by Fund members.

If, as a result of adverse selection, the average cost of new DBD entrants became greater than the 21% of salary amounts contributed to the DBD, it is likely that the DBD would need to be closed to new employees to ensure that the financial security of existing DBD members would not be compromised. This would lead to a loss of a very good superannuation choice as a unique offering by the higher education sector.

We also note that that the issue of *new employees who are not existing defined benefit members but who are eligible to join a defined benefit scheme* (from paragraph 1.30 above) is likely to apply only to UniSuper as we are one of the only – if not the only – open, private sector defined benefit funds.

It is salient to note that contributions to many Commonwealth, State and Territory defined benefit schemes have been deemed to be made in compliance with the choice of fund requirements by section of 15 the Superannuation Guarantee (Administration) Regulations 2018.

Public offer status and UniSuper

While UniSuper has a public offer licence, we restrict membership to those who work (or have worked) in the higher education and research sector, plus their family members. We regularly review this position and the Board has recently reaffirmed that this continues to be in the best interests of our members.

Even with our restrictions on eligibility for membership, the DBD is only available to permanent employees working in the higher education sector. For example, family members cannot join the DBD.

If UniSuper were to allow broader membership availability in the future, it would not be actuarially or practically feasible for any of that broader membership group to be eligible to join the DBD – they would all become Accumulation members. As a result, expanding our public offering to the broader public would have no impact on the DBD or the selection risk in respect of the DBD.

In conclusion

Should the Bill be adopted in its present form, UniSuper and its members would be exposed to elevated risks, risks which are avoidable while retaining the legislation's underlying objective to provide choice to individuals. As a result, we strongly suggest that the Committee recommend that:

- The current exemption from the choice of fund requirements for *existing* defined benefit members should continue; and

- An exemption for those who are *newly* eligible to become defined benefit members should also be provided for in the legislation.

Should the above be adopted, those who are eligible to become defined benefit members would continue to be defaulted into UniSuper's DBD.

But all such individuals would have the ability to

- opt out of the DBD within 24 months if they would prefer an Accumulation arrangement, and
- opt out of UniSuper into a different superannuation fund (as would be enabled for any non-defined benefit member under this Bill).

This could be thought of as a model of “deferred choice” and would ensure that we could continue offering our strong and valuable defined benefit scheme to new members.

Thank you for the opportunity to provide comments on this Bill. Should you wish to discuss these comments, I can be contacted on [redacted]

Yours sincerely,

[redacted]

Kevin O’Sullivan
Chief Executive Officer

APPENDIX – ADDITIONAL INFORMATION RE UNISUPER EXPERIENCE

1. Contributions to UniSuper

DBD members:

Employer contributions of 14% of salary are made to the DBD in respect of permanent employees in the DBD. These members generally also receive an additional 3% (i.e. for a total employer contribution of 17%) to an Accumulation 1 account.

In addition, these members contribute an additional member contribution of 7% of salary. But they do have the flexibility to reduce their contributions below the standard 7% rate. At present, the vast majority of DBD members contribute at the full 7% rate. Where a member reduces their member contribution rate, the additional 3% employer contribution is redirected to the DBD and DBD benefits are appropriately adjusted.

Accumulation 2 members:

Permanent employees generally receive 17% employer contributions, paid to their Accumulation 2 account.

These members also have a standard additional member contribution of 7% of salary, but a larger percentage of Accumulation 2 members (about 70%) opt to reduce their member contribution rate compared to DBD members (about 36%).

Accumulation 1 members:

Most fixed term contractors now receive 17% employer contributions, paid to their Accumulation 1 account. Other employees, typically casuals, receive contributions at the legislated SG level

2. Benefits provided within UniSuper's Defined Benefit Division

At retirement or resignation, members receive the sum of their Defined Benefit component and their accumulation account.

For members who join the DBD after 1 January 2015, the defined benefit component is determined based on the following formula:

5-YEAR BENEFIT SALARY	The member's average salary over the last five years when contributing to the DBD
×	
BENEFIT SERVICE	The length of time as a DBD member
×	
LUMP SUM FACTOR	Based on the member's age at exit
×	
AVERAGE SERVICE FRACTION	This reflects the member's level of full-time/part-time employment
×	
AVERAGE CONTRIBUTION FACTOR	This reflects the member's level of member contributions to the DBD

For members who joined the DBD prior to 1 January 2015, the above formula applies in respect of their DBD membership period from 1 January 2015. In addition, their benefit <u>in respect of service prior to that date</u> is calculated similarly with the exception of the use of their 3-Year Average Benefit Salary at the date of exit, instead of their 5-Year Average Benefit Salary.

And members who joined the DBD prior to 1 July 1998 are entitled to opt for an indexed lifetime pension, the initial amount of which is calculated similarly to the lump sum benefit but using Pension Factors instead of Lump Sum Factors.

Examples of the age-based Lump Sum Factors and Pension Factors are as follows:

Age	Lump Sum Factor (%)	Pension Factor (%)
40 or less	18	N/A
45	19	N/A
50	20	N/A
55	21	1.3
60	22	1.5
65	23	1.7
70	23	1.9

If desired, we will provide UniSuper's *More about the DBD and Accumulation 2* booklet, which contains a full explanation of these formulas and detailed examples.

When a member joins the DBD, he or she automatically becomes entitled to additional benefits payable in the event of death or disablement. These benefits also are calculated based on formulas.

The total contributions of 21% of salary cover the retirement, resignation, death and disablement benefits, as well as any contribution tax payable. There are no deductions to DBD member accounts for this cover.

3. Membership and assets in each Division of UniSuper (as at 31 December 2020)

		Funds under Management ($ Billion)		
UniSuper Product	**# of Members**	**Total**	**Accumulation**	**DBD**
DBD	93,046	31.1	8.5	22.6
Accumulation 2	21,804	8.8	8.8	
Accumulation 1	342,839	26.7	26.7	
Total in accumulation phase	**457,689**	**66.6**	**44.0**	**22.6**
Flexi Pension (account-based pension)	22,810	12.6	12.6	
Indexed Pension	8,505	6.5		6.5
Total - pension phase	**28,226**	**19.1**	**12.6**	**6.5**
Total	**468,675**	**85.7**	**56.6**	**29.1**

4. Transfers from the DBD to Accumulation 2 over the past five years

Calendar Year	# of Members	Total Assets ($m)	Average account balance ($)
2015	1,737	31.1	17,879
2016	1,592	32.2	20,250
2017	1,986	30.9	15,557
2018	2,384	39.0	16,354
2019	2,596	46.0	17,706