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SUBMISSION 68

Industry Funds Forum Inc.

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The Committee Secretary
Standing Committee of Economics, Finance and Public Administration
Department of the House of Representatives
Parliament House
CANBERRA ACT 2600

By email to: efpa@reps@aph.gov.au

ATTENTION MS BEV FORBES

Dear Ms Forbes,

INQUIRY INTO IMPROVING THE SUPERANNUATION SAVINGS OF PEOPLE UNDER AGE 40

The Industry Funds Forum (IFF) made a submission to this inquiry on the 22 July 2005 and gave evidence at the Melbourne hearing on the 3 February 2006.

The IFF was asked at the hearing to make a further supplementary submission outlining the initiatives of industry superannuation funds with respect to finding 'lost' superannuation, minimising duplicate accounts and increasing consolidation, and suggested improvements to better manage these issues, including the establishment of a centralised Eligible Rollover Fund. The IFF was also asked to provide any information or evidence that illustrates the impact of commissions on compulsory superannuation.

Attached please find the IFF's supplementary submission addressing matters relating to the management of 'lost' superannuation and the management of duplicate accounts and consolidation. Attached to this submission is an Appendix prepared by professional financial planners Industry Fund Financial Planning showing the impact of commissions on compulsory superannuation.

The IFF would be pleased to discuss this supplementary submission, including the Appendix, or its primary submission, and provide any further information required by the Committee in order to assist it with its deliberations around improving the superannuation savings of people under age 40.

Thank you for the opportunity to contribute to these discussions.

Yours sincerely,

IAN SILK
Convenor
Industry Funds Forum

INQUIRY INTO IMPROVING SUPERANNUATION FOR PEOPLE UNDER AGE 40

Supplementary Submission from the Industry Funds Forum

The Industry Funds Forum welcomes the opportunity to provide a supplementary submission to the Inquiry into Improving Superannuation for People Under the Age of 40 in relation to the management of 'Lost Super', duplicate accounts and consolidation.

About the Industry Funds Forum
The Industry Funds Forum (IFF) represents the interests of 24 major industry superannuation funds, their members and employers. These funds have more than 8 million members (approximately 5.2 million of these members are under age 40), \$68 billion in assets and over 450,000 participating employers.

Industry Fund Initiatives to Reduce 'Lost Super' and Duplicate Accounts, and Increase Consolidation
The majority of these funds use AUSfund as their ERF. AUSfund is a not-for-profit fund with 29 fund clients that are industry or public sector funds and 1.65 million members with \$559.4 million in assets (average account size of just \$339). Almost half of the membership of AUSfund is under the age of 40 – 10% under age 25 and 38% in the age group 25-39. AUSfund undertakes extensive and successful activities in reuniting members with their active superannuation account. These activities have resulted in AUSfund finding almost 500,000 lost members and reuniting a further 250,000 of its members with assets of \$100 million, with their active superannuation through consolidation programs. AUSfund developed the proposal that led to the establishment of the very effective Australian Taxation Office (ATO) matching program, pioneered by AUSfund.

These and other highly successful initiatives of industry funds (detailed throughout this paper) give IFF a unique perspective on issues associated with lost superannuation, duplicate accounts and consolidation.

Notwithstanding this work, there still remains more than \$8.2 billion of superannuation paid into the ATO and 5.4 million members reported on the Lost Member Register (LMR) – and the implication of the recent Australian National Audit Office (ANAO) report on the LMR is that this figure is significantly under reported.

The lack of a systematic approach to lost and inactive superannuation, especially where small accounts are involved, has contributed to the growth of monies reported on the LMR.

The success of industry fund activities suggest that the replication of the AUSfund approach in all ERFs would reduce the incidence of lost superannuation to a very large extent.

Very significant further reductions could be gained if these activities were coupled with increased use of Tax File Numbers (TFNs) and the automatic consolidation of inactive superannuation accounts after two years of inactivity to the owner's most recently active account (with appropriate safeguards to protect insurance and to give an opt out). The effectiveness of these programs would be greatly enhanced if they were linked with a strong reporting and enforcement regime.

IFF member funds undertake regular searching, matching and consolidation activities as part of their strategies to manage small accounts and lost members. These include:

- ATO Matching
- Cross Fund Matching
- Address Matching
- Duplicate account matching

Fund members are advised in the Annual Report Member Guide Product Disclosure Statement.

ATO Matching
ATO Matching is a process initiated by an IFF member fund that uses member details to search for and retrieve lost or unclaimed money held on a member's behalf in one of the ATO managed funds. Funds conduct a matching exercise aginst the ATO database for the Superannuation Guarantee (SG), Superannuation Holding Accounts Reserve (SHAR) which between them have $8.2 billion and the 'Lost' Member Register which has over 5.4 million names on it.

This process, which commenced in December 2003 has now become a regular activity of most IFF member funds. The frequency of the matching exercise has increased and this year most funds are expected to conduct this search three times during the year.

The first search of the LMR conducted one of the larger funds (with over 83% of its membership under age 40) which had 600,000 members with TFNs resulted in almost 30,000 consolidations. These 'lost suer' accounts were consolidated into the members' active superannuation fund, with the members' knowledge. This fund now conducts monthly searches for some 10-12,000 members with good success.

Another fund (with 77% of its membership under age 40) which has undertaken this activity three times, has had the following results:

Transaction	Number of members	Dollar Value
LMR	15,427	$27,456,404.86
SG	13,402	$5,601,009.89
SHAR	7,331	$2,142,486.37

The total value of the assets of members with lost accounts located through these activities for just one fund, which at this stage has only carried out matching activities three times is $35.2 million.

Cross Fund Matching
Funds that use AUSfund as their ERF to manage small inactive accounts are able to use a process established by AUSfund that allows for cross fund matching with the originating fund. This process identifies members that have become active, after a period of inactivity where there small inactive accounts was transferred to AUSfund, and the small balance is redirected to the originating fund where the account has been reactivated.

This process which is very successful in eliminating duplicate accounts and reducing lost super accounts, commenced about four years ago and is used regularly by AUSfund clients.

One fund that started this process in November 2001 and normally conducts the process once per year has located the following in lost super and reunited these funds with the active super account to avoid duplicate members:

Number of members transferred	Dollar Amount transferred
42,330	$15,816,270.13

Address Matching
Most industry funds use a range of processes for locating lost members, including those conducted through AUSfund and the ATO. This include 'free of charge' address notification change with mail redirection notices lodged through Australia Post, some use private location companies to find the current address for members without a valid address on file. These companies have had reasonable success funding about 23% of the addresses for those lost but they can be costly.

Location activities undertaken by funds could be greatly assisted by limited and controlled use of information available to the more easily and correctly identify lost members and in many cases save costs and the need to transfer members' accounts to any ERF. In many cases these activities could be undertaken by the fund.

Duplicate account matching
The administration system of most industry funds have inbuilt functionality that enables the identification of any member that is on the system more than once. If a member already exists on the database and a new record is created with the same or similar details, the two records are flagged and a process to determine and identify if they are the same person is undertaken. This involves reviewing the member's personal details (name, address, date of birth, beneficiaries) as well as their employment history to determine if the member is receiving contributions to the two accounts.

Once it is determined that the two accounts are for the same person, the accounts are merged into the original account. All current member details are updated in the merging process. This avoids members having two accounts with small balances and being charged two sets of fees. The administration system automatically reverses all fees in relation to the duplicate account and makes any adjustment of interest, and merges the account balances of the member into the original account.

Other Activities to Manage Duplicate Accounts and Help Reunite Members with their Lost Members

The following tasks are also performed as part of the administration of most industry superannuation funds:

- A mail out is conducted twice a year before the Annual Benefit Statements and Record of Contributions are mailed to members. A letter is sent to employers who have employees with an invalid address, to seek confirmation of the new address for the employee. In some cases this is followed up with a telephone call if the employer fails to respond.

- Each time an employer receives a Contribution Advice listing their employee's details, the employer is requested to provide the correct address for any member without a valid address.

- Employers who make a contribution are issued with a Confirmation Advice letter. This letter includes a request to supply the correct address for employees without a valid address.

- Funds mail a statement to members twice per annum – the Annual Benefit Statement at the end of the financial year and the Record of Contributions shwing all contributions received during the first six months of the financial year. These are mailed to members at their home address. This mail out includes a magazine which often contains stories emphasises how important it is to maintain a current address, how to look for lost super, the importance of consolidating super etc. This magazine contains a coupon as does the statement usually to make it easy for members to advise the fund of their change of address.

- Where mail is returned for a member and the fund has an email address (which are greatly increasing in number) for the member, an email is sent to the member asking them to advise the fund of their new mailing address.

- Call Centre staff ask members to confirm their address each time they talk to members and this process picks up many new addresses.

- Member application forms include a declaration that authorises the Fund to search for lost super on a member's behalf.

- Some funds provide facilities such as a "Find your lost super" form which is located on their website for members who have not provided their TFN or who have not filled out an application form.

- Fund search the ATO registers (LMR, SHAR, SG), some monthly for those new members who have provided a valid Date of Birth, Address and Tax File Number. If super is found in the SG and SHAR records, payment is made directly to the member's account, however, if super is found in the LMR, funds will write to members, letting them know they have found 'Lost super'. Generally they provide a pre-populated form to encourage members to initiate the transfer.

- Industry funds run regular 'Lost super' campaigns in newsletters and annual reports to encourage members to provide their TFN if they have not already done so and to check for their lost super via the website.

- Industry superannuation funds initiated and successfully conducted in conjunction with the ATO a number of events in shopping centres around the country where consumers could approach operates who would look for their lost super. These events located many millions of dollars in lost super and helped to raise the consciousness of many consumers about the need to manage and stay in touch with their superannuation.

One Centralised Eligible Rollover Fund

The establishment of one centralised Eligible Rollover Fund would reduce the number of inactive accounts as duplicate accounts could easily be consolidated.

AUSfund has very effective location and consolidation programs, unlike most ERFs which simply serve as a dumping ground for small inactive accounts. Most ERFs do little to locate lost members or consolidate accounts. AUSfund's consolidation programs include consolidation of multiple inactive accounts within AUSfund and where an inactive account with AUSfund becomes active it is transferred back to the originating fund so the member can benefit from the full range of services and benefits.

A centralised ERF with a specific mandate to undertake searching, matching and consolidation activities could ensure that proper scrutiny could be given to all lost superannuation monies once transferred to the ERF. This would need to be supported by a transfer policy for lost superannuation accounts so that funds who have failed to locate a member are required to transfer the account to the ERF so it can be included in searching, matching and consolidation activities.

As an ERF, all members' accounts are protected from erosion from administration fees in accordance with the Superannuation Industry (Supervision) Act 1993. However, most ERFs deduct a percentage fee for administration fees and these can be high and over time can significantly diminish the value of an account. AUSfund charges a flat dollar fee rather than a percentage fee which is much lower than the fee charged by a superannuation fund (even an industry fund which has low fees) as the ERF has limited ability to service many of its members through the issue of statements and reports as there is no current address on file for the member.

A centralised ERF could achieve significant economies of scale, while still applying an equitable dollar based administration fee, ensuring the integrity at intended member protection rules.

Multiple accounts result in fragmentation and reduction of retirement savings for members, and this in turn can result in reduced planning and involvement by the member. Multiple accounts can also create inefficiencies for the superannuation industry, as this can result in increased numbers of small accounts, multiple administration fees and increased member protection costs. One centralised ERF increases the prospects for merging more duplicated accounts.

Individuals are more likely to have a sustained interest in their superannuation benefit when various accounts have been consolidated to produce a larger balance. Larger average balances in a centralised ERF could be promoted to encourage people to search for their lost superannuation. Members are presently confused about where to start to look for lost superannuation. If there was one centralised fund this could be well promoted and members would know where to go to look for any lost superannuation.

ERFs have been established in part to assist superannuation funds in responding to the requirements of member protection and to manage this very significant cost, which is borne by all superannuation fund members. If an ERF acts solely as a repository for small, lost and inactive accounts, then it provides little benefit for the members who do not know the ERF holds monies an account for them.

One central not-for-profit ERF that actively re-unites members with their active superannuation account will benefit lost members and small account holders, and at the same time result in cost savings to all superannuation fund members who pay the cost of member protection and lost member management. The current system, which does little to address the problem of the growing accumulation of lost and small accounts (which can have significant total assets) only benefits ERF shareholders and their service providers who profit from these businesses. Any centralised ERF should be a not-for-profit fund because a commercial ERF, which needs to make a profit for its owners would find it very difficult to provide an effective and low cost service consistent with the Government's policy of protecting small accounts.

As the majority of funds recorded on the Australian Taxation Office's Lost Member Register are located within ERFs, this is a significant portability issue for the superannuation industry. If there was a centralised ERF it would be more administratively straightforward for that body to work with the ATO and to provide the ATO with an annual report of all member details (including Tax File Numbers) to allow for easy consolidation of accounts with members' active superannuation account using information required for matching available through the ATO.

The ATO can also utilise its current surcharge database to identify those members of a centralised ERF with active superannuation accounts where a contribution was received during the reporting period (other than defined benefit accounts). The ATO could report to the centralised ERF listing details of the active superannuation fund for matched members. Where a member received contributions in more than one superannuation fund during the reporting period, the ATO report should list the most recent contribution received. Upon receipt of this report, the centralised ERF should be required to transfer the matched account to the relevant superannuation fund. The centralised ERF or the receiving fund or both, may be required to advise the member of the transfer. It is further recommended that the transfer of benefits take place no more than 90 days from the date of receiving the ATO report.

There are few administration issues associated with this approach. ATO reporting that requires the interrogation of the whole of a fund's database already existing as it was created for the administration of the surcharge. Transfer protocols already operate between many superannuation funds, and electronic transfers of member account details and fund benefits also operate routinely in many cases.

While this approach could work with the whole universe of ERFs it would be more straightforward and economical if the processes were centralised in one ERF and education of members would be simpler and less costly.

How could the system be improved?

- Clarify immediately the application of the definition of Lost Member
  There is a great deal of confusion about the definition of a 'Lost Member' and funds are doing different things in relation to implementing these regulations. Some understand believe that the definition of 'Lost Super' requires all members who have not received a contribution in the two years prior to be reported to the ATO register, regardless of the fact that these members have a current address on file and do not consider themselves to be lost and nor does their superannuation fund who is in regular contact with them. These funds are reporting these members to the LMR and this is greatly inflating both the

numbers of 'Lost Members' on the register, and to an even larger extent, the value of "Lost Super" as some of these accounts are very large.

Other funds are not reporting these members because they do not believe they are lost.

IFF has raised this important matter with regulators on a number of occasions and it remains a continuing problem. Regulators will not give a clear direction to funds and nothing has been done to clarify this definition.

A clear definition of a 'Lost Member' could be done immediately and at no cost, in fact it would save a great deal of money on unnecessary reporting and would greatly reduce the value of 'Lost Super' from its current $8 billion.

- The ATO or a centralised ERF would be in the best position to reduce the amount in the LMR as it has access to all member account details, including ERF accounts, and could use this information to write to members encouraging them to consolidate into their active super account. With some consultation with industry, if a person completed a prescribed ATO form, funds could agree to consolidate. This could be done on an opt-out basis, keeping the spirit of choice and portability.

- Superannuation funds are not in a position to do this because they are hampered by the legislative requirements for portability, which requires the transferring fund to write to the member to advise them they have the right to ask for more information. A member either has to ask for more information or sign a form to say they waive this right, before the transfer can be completed. If a member has multiple funds, this could become a lengthy process with a diminishing chance of consolidation.

- If the inactive accounts of members with a valid address were removed from the LMR, the numbers would reduce dramatically. The ATO could use TFNs to locate members with SG or in SHAR and transfer this money to their active superannuation fund. The ATO could also search for all existing accounts, writing to members on the LMR and encouraging them to consolidate to their active superannuation account.

- Where no TFN has been supplied, the ATO is, once again, in a better position than superannuation funds to encourage consolidation. Funds often do not have comprehensive information for each member's account so it is difficult to facilitate an accurate consolidation process for all members. A great deal of work is done by funds as outlined earlier in this submission but more could be done by the ATO as they have more reliable and comprehensive information to enable a quality search and consolidate process to be undertaken.

- Transfer protocols developed and used mainly by industry funds should be a standard across the industry as these help streamline and speed up the consolidation process. Many members find they need to constantly chase the transferring fund as these transfers take far to long to enact. Some members report that they repeatedly call and write to the transferring fund chasing these transfers before finally giving up. This is a great waste of effort and money and does nothing but reduce efficiency in the industry and give consumers to wrong message about consolidating.

- ERFs should be mandated to perform minimum prescribed efforts to find members.

- Credit reference checking facilities may offer an opportunity to locate 'Lost Members' although IFF enquiries indicate that these facilities can only be used if a person owes a debt rather than when they have an entitlement. It is recommended that further enquiries be made about using these facilities to help identifying "Lost Members'.

- A review of the compliance to reduce the burden on funds and to encourage greater efforts in consolidating superannuation found as lost.

- Finally, by the establishment of a centralised not-for-profit ERF with the powers to efficiently search, match and consolidate superannuation.

APPENDIX

THE IMPACT OF COMMISSIONS ON COMPULSORY SUPERANNUATION

PART OF THE INDUSTRY FUNDS FORUM SUPPLEMENTARY SUBMISSION TO THE INQUIRY INTO IMPROVING THE SUPERANNUATION SAVINGS OF PEOPLE UNDER THE AGE OF 40

Prepared by Industry Fund Financial Planning

The Effect of Contribution Fees on Final Superannuation Balances

Currently in Australia there are many Superannuation products that allow advisers to debit commission from Government-mandated contributions. This paper examines the effect of commission being deducted from the final balance.

Case Study

We have considered an actual member who recently approached us to review her current Superannuation arrangements. The facts were:

- Her employer contributed $1,000 per month to one fund.
- The adviser, her accountant, is being paid 5% of each employer contribution.
- The client was unaware that any commission was being paid until we highlighted the deduction.

Employer contributions

The employer contributed $20,000 during the 04-05 financial year, from which 5% or $1,000 initial commission was debited. We have modelled the effect on the final balance, of this commission debit.

Assumptions

- Current age: 48 years.
- Current balance: $92,000
- Employer contributions of $20,000 per annum (paid monthly), which are constant, and continue until age 65.
- Fund earns 6.25% net.
- We have used identical investment and monthly administration fees for the purpose of this comparison. (This is unlikely to be the case however we are measuring the effect of the initial commission on the final balance).
- Amounts have been rounded to the nearest $1,000.

Age	Balance (No commission) $	Balance (5% initial commission deducted) $	Difference
50	124,700	123,600	-1,100
55	225,000	220,600	-4,400
60	358,600	349,800	-8,800
65	536,600	521,900	-14,700

The difference over 27 years is $14,700.

What If ....

Commission had been debited from age 30, with exactly the same parameters. In this case, this is reasonable given the skills of the individual. The final balance would be reduced by $57,000 due to the commission being deducted.

Summary

The effect of initial commission being debited from Government-mandated Superannuation contributions, compounds the longer it occurs. We would be happy to model any number of scenarios as required.

Francis Gayton, B.Ed., DipFP.
Head of Practice
Industry Fund Financial Planning
A division of Industry Fund Services Pty Ltd
AFSL 232514
9/2/06

Attachment: Copy of Member transaction statement (PDF format).

Glossary:

Initial commission: debited from the employer contribution at the outset. Typically commission if debited will be in the order of 1% - 5%.

MER (management expense ratio – also called ongoing management charge): an estimate of the total percentage cost of all charges debited from the average balance.

Trailing commission: a percentage of funds under management paid to an adviser. Typically this ranges from 0.25% - 0.6% of total funds.