



**Guided
Decisions**

House of representatives Standing Committee on
Economics, Finance and Public Administration

Submission No: 46

Date Received: 12/9/05

Secretary: JRS

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9th September 2005

SUBMISSION 46

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

Email: efpa.reps@aph.gov.au

Dear Sir/Madam

Inquiry into improving the superannuation savings of people under 40

Guided Decisions is pleased to provide a submission to the Committee's inquiry into improving the superannuation savings of people under 40.

Guided Decisions is an Australian privately-owned company specialising in developing integrated mass market advice services and processes for financial services companies. These services and processes enable financial institutions to help guide their customers to make better informed financial decisions.

We would be pleased to discuss this submission or provide further information as required by the Committee in order to assist it with its deliberations around Improving the Superannuation Savings of People Under Age 40. Please contact us on 03 9614 0207 or by email: inquiries@guideddecisions.com.au.

Yours sincerely

Danny Shuttleworth
Principal



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Submission to

**House of Representatives Standing Committee on
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**Inquiry into Improving the Superannuation
Savings of People under 40**

By

Guided Decisions

August 2005

Overview

The vast majority of Australians are still not saving enough to support a comfortable lifestyle in retirement – the current 9% employer contribution is, by itself, not enough.

There is now significant data and research available, both in Australia and overseas, to demonstrate that information and education alone will not overcome consumer apathy when it comes to retirement savings. Furthermore, in Australia there is too large a gap between the provision of the information/education and face-to-face advice. In some cases current legislation is working to widen this gap.

In our view, the retirement savings patterns of those people under 40 will only improve by enabling the integrated provision of information, education, guidance tools and advice. This submission focuses on expanding on these points and highlighting ways to effectively fill the education – advice gap that exists today.

The Education – Advice Gap

Australia has a complex superannuation system that is extremely difficult to navigate through alone without guidance and advice. However access to this advice comes at a relatively high cost because of the existing regulatory framework designed to protect the public's rights and interests.

Most people under 40 do not access advice, but are provided with information and education by their Super Fund. An Industry Fund research study¹ assessing member opinion of information and educational material showed most (53%) read less than half of what is sent to them, let alone understand and then act on the information. Similar findings in the US by Hewitt Associates found that “while knowledge and education are important for building a foundation for change, they're clearly not enough to influence some groups of employees - particularly low savers - to contribute more to their 401(k) plans.”

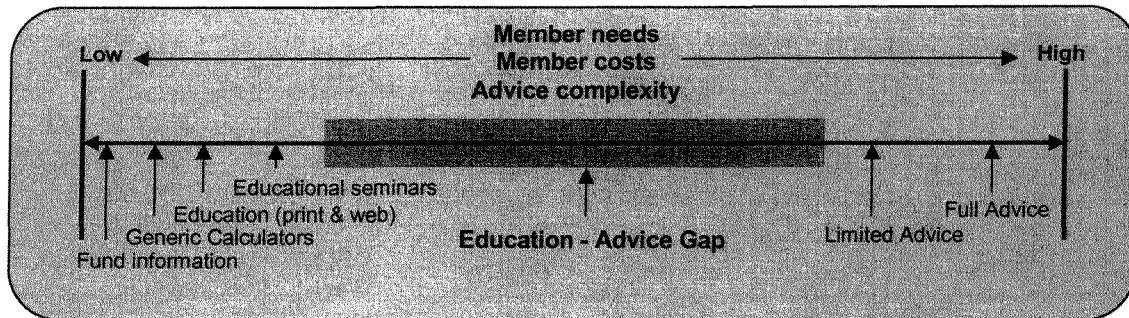
The Industry Fund study also showed that most people had identified the need for guidance or advice with 74% of members stating that they would choose a fund offering “free” financial planning advice. Importantly, this need for advice has also been identified by retirees in a recent Newspoll survey which found one third of Australia's 4.8 million retirees regret not having sought expert financial advice during their working lives, while 35% wish they had started saving for retirement earlier.

The spectrum of alternatives for Super fund members is they can choose to self-educate or they can pay for advice. For the vast majority of Australians it is easier to make no decisions and take no action, whereby they accept default portfolios and have no more than the mandatory 9% SG contribution to their Super Fund until they can afford advice. For many this will be too late and they will be under-funded for their retirement.

In the Australian Superannuation market there is currently a very wide education - advice gap that needs to be filled so that members can achieve their retirement goals.

¹ 2004 Members' Education research conducted by Roberts Research Group

Education - Advice Gap:



A little guidance in the early years can make a significant difference

With the recent arrival of Superannuation Choice, a lot of industry debate has focused on fund fees. Fund fees will have an impact on a person's overall superannuation balance at retirement, however our analysis shows personal strategic decisions are likely to have a far greater impact on whether a person achieves their retirement goals.

Personal strategic decisions are important decisions or choices that a superannuation member needs to make based on their own circumstances. These decisions include:

- **Goal setting** – determining their preferred retirement lifestyle and how much they will need to live that lifestyle throughout their expected retirement.
- **Retirement Funding** – determining whether they are and/or, continue to be on track to meet these goals – and if not, what they need to adjust to get back on track.
- **Contributions** – deciding how much they need to contribute and what is the best way for them to contribute.
- **Asset allocation** – choosing the right portfolio to match their personal risk profile.

If people under 40 get these decisions right in the early years, it will make a significant difference to their success in meeting their retirement goals and the amount of money they have available in retirement. See Case Study 1 – Asset Allocation.

Case study 1 – Asset Allocation

A 22 year old female, commences work earning \$30,000 pa. Typically she would have an aggressive risk profile with a long investment time horizon and would most likely be advised to go into a Growth portfolio.

Project forward 43 years when she retires at age 65, the difference in total retirement benefits would likely be 10%-15% for the Growth portfolio compared to the default Balanced portfolio.

Anecdotal evidence suggests that the majority of members in corporate and industry funds are invested in the default Balanced portfolios.

The need for guidance or advice has an equal level of importance when it comes to contributing to Super – see Case Study 2.

Case study 2 – Super Contributions

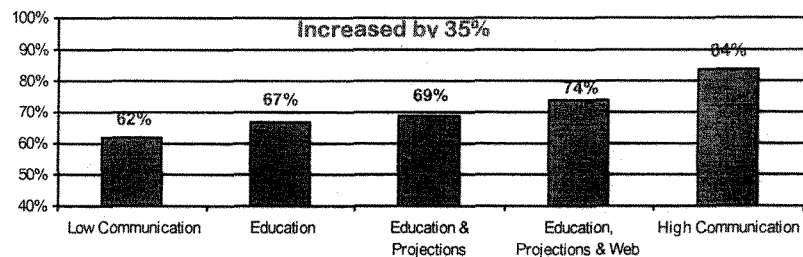
A 30 year old male, earning \$28,000 pa, has a spare \$20 per week. The conventional thinking espoused by many is that he should pay off any outstanding debt. Yet if he contributed this \$20 a week via a voluntary contribution to Super, he would receive a Government co-contribution of \$1,500 into his super account. That's a return of up to 150% even before the benefits of favourable taxation or portfolio returns are considered. If his personal circumstances changed, he may wish to consider other ways to contribute to super, such as making a spouse contribution or by salary sacrifice.

US Experience & Learnings

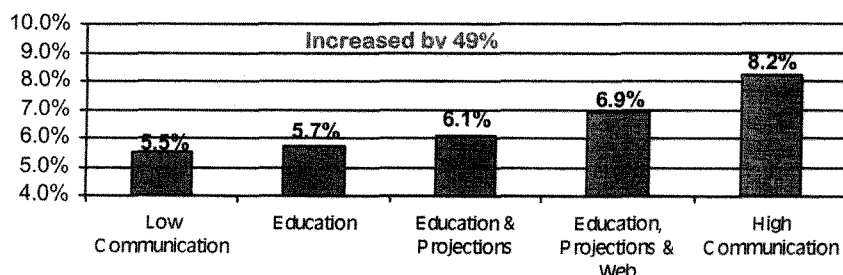
In the US, within the 401(k) retirement savings system new advice models have evolved to meet the needs of Plan members and have had increasing levels of acceptance.

A study of 48 different company plans encompassing over 300,000 employees measured the effectiveness of the different communication, education and guidance programs on both participation in the Plans (as the US 401(k) system is an opt in system) as well as contribution rates from existing Plan members². This study found that those Plans that offered High Communication programs (ie. integrated education, personalised projections, internet guidance tools) facilitated a 35% higher participation rate and a 49% higher contribution rate than those Plans that offered basic Plan information to their members.

Participation Rates:



Contribution Rates:



² 'The Importance of Financial Communication for Participation Rates and Contribution Levels in 401(k) Plans', The Wharton School, University of Pennsylvania

In the US, personalised projections are one of the most commonly used guidance tools. One of the most popular guidance and advice providers recently stated that they give each of its 401(k) members a personalised statement showing the member's account status and how a particular action such as a higher contribution, would impact take-home pay and future retirement savings. "We don't want to kill people off with reams of data," they stated. "We want to do a simple gap analysis. At the very least, it gets people to question: Am I on track?"

Issues and Recommendations

Personalised Product Projections

Under the current arrangements, the fact that 9% will not be enough to fund a comfortable retirement lifestyle will come as a shock to many people. Currently they are never told what their super savings are likely to amount to. Every year they receive a statement from their super fund which tells them how much they contributed, what the fund's investment earnings were and what the balance of their super account is. The problem is this is all looking backwards.

An employee could be almost at retirement with what they believe is a sizable super sum only to then realise that the funds are insufficient to meet their retirement goal. At this stage it is almost impossible to make amends and goals have to be significantly changed.

Personalised product projections are used extensively overseas. One of the reasons they are not widely provided in Australia is that product specific projections result in the provider deemed to be giving '*financial product advice*'. The provision of financial product advice results in having to meet appropriate regulatory requirements (eg licensing, disclosure etc.).

These personalised product projections are also likely to be deemed '*personal advice*'. The provision of personal advice comes with an additional set of requirements relating to the suitability of the advice and associated disclosure requirements.

This results in quite onerous responsibilities for simply providing personalised product projections to a fund's existing members and few, if any, projections are currently provided to members.

Recommendation -

Enable the production of Personalised Product Projections

Existing members of superannuation funds need to be able to regularly assess their likely level of benefits on retirement. They need to be able to do this so they can determine if they are on track to achieve their retirement goals and if not, make the necessary adjustments early enough. The value of such projections in changing member behaviour is demonstrated in overseas markets.

We need to find ways to enable the provision of standardised projections in Australia so that they become an integral part of our member reporting.

Effectiveness of guidance tools

Internet access and usage in Australia is amongst the highest in the world and indeed well over 50% of Australian households now have home internet access. This provides an excellent opportunity for delivery of cost effective guidance to members.

However, in a number of instances (e.g. superannuation calculators and risk profilers) ASIC has indicated that it considers the close linkage of financial product information with generic calculators results in these calculators becoming product-specific calculators.

This again has financial product advice and personal advice implications and results in quite onerous responsibilities for fund's wishing to provide effective guidance tools to their existing members.

Recommendation - Enable the provision of effective guidance tools

We recommend that appropriate relief be provided to funds offering product-specific risk profilers and other guidance tools to their existing members (i.e. for non-marketing purposes).

It should be noted that ASIC is seeking to reduce uncertainty about how the law applies to online calculators and seeking to promote access to such tools. It is currently consulting on proposed relief and guidance for online calculators. In our view this relief needs to go further than is currently proposed to facilitate both of the recommendations above. We will be making a detailed submission to ASIC in this regard.

Distinguishing between servicing existing members and attracting new members

A common theme arising from the recommendations above is that currently there is no distinction made between the provision of guidance tools/materials for existing members of funds and their provision in marketing and promotional campaigns.

Projections have been misused in the past to attract investors to financial schemes and we recognise the need to protect investors against this happening in the future. However in the case of existing members we believe great assistance can be provided by the provision of standardised projection and guidance tools.

One way of addressing this dilemma may be to create a distinction between existing members and prospective members and treat these two categories differently in any reliefs granted or in revisions to the existing regulatory framework.

Costs of advice

Recent regulatory changes, including FSRA, have increased the compliance responsibilities on financial advisers and their costs for dealing with individual clients. This results in advisers understandably focusing on those customers with more substantial wealth savings who are normally aged over 50.

ASIC is currently conducting a series of financial services refinement projects and one of the intentions of these initiatives is to reduce the compliance burden on the industry. This could assist in lowering the cost of delivery of advice. Such initiatives should be continued.

In our view consideration should also be given to offering a tax deduction for advice on superannuation. This would effectively reduce the cost of advice to members and help to narrow the gap we highlighted earlier, between full advice provision and basic education materials.

About Guided Decisions

Guided Decisions specialises in developing integrated guidance and advice services and processes for financial services companies. These services and processes enable financial institutions to help guide their customers to make better informed financial decisions.

Our executive team has extensive experience in Superannuation, Funds Management and Banking. Professional backgrounds include actuarial, financial planning, marketing and senior executive management.

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