The Senate

Select Committee on Superannuation

Draft Superannuation Industry (Supervision) Amendment Regulations 2003 and draft Retirement Savings Accounts Amendment Regulations 2003

September 2003

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MEMBERSHIP OF THE COMMITTEE

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Senator Penny Wong		(South Australia, ALP)

Secretariat

Acting Secretary	Stephen Frappell
Executive Assistant	Dianne Warhurst

Address: Senate Select Committee on Superannuation
Parliament House
CANBERRA ACT 2600

Telephone: (02) 6277 3458

Facsimile: (02) 6277 3130

Email: super.sen@aph.gov.au

Internet: http://www.aph.gov.au/senate_super

TERMS OF REFERENCE

That the draft Superannuation Industry (Supervision) Amendment Regulations 2003 and the draft Retirement Savings Accounts Amendment Regulations 2003 be referred to the Select Committee on Superannuation for inquiry and report by 21 August 2003, with particular reference to:

a) the extent to which portability of superannuation benefits already exists;

b) the role of current, and likely future, barriers to portability, including exit fees;

c) the desirability and practicality of the portability regime contained in the draft regulations, particularly in the context of the existing structures of the superannuation and financial planning industries; and

d) additional consumer protection measures.

CONDUCT OF THE INQUIRY

On 17 June 2003, the Senate referred the draft Superannuation Industry (Supervision) Amendment Regulations 2003 and the draft Retirement Savings Accounts Amendment Regulations 2003 to the Senate Select Committee on Superannuation for inquiry and report by 21 August 2003. That reporting date was subsequently deferred to 10 September 2003.

The Committee wrote to a large number of parties potentially interested in the inquiry on 20 June, inviting them to lodge a submission by 18 July 2003. In addition, the Committee advertised its terms of reference widely in the press in early July.

The Committee received 33 submissions from a range of individuals and organisations. They included peak industry bodies, superannuation funds or fund trustees, professional financial organisations, financial service providers, peak employee groups, peak employer groups and the relevant government agencies. A list of submissions is at **Appendix One**. The submissions are available electronically at the Committee's web site at www.aph.gov.au/senate_super.

The Committee subsequently conducted the following hearings:

Thursday 31 July 2003 – Sydney
Friday 1 August 2003 – Melbourne
Wednesday, 13 August 2003 – Canberra

The Committee notes that during the Committee's hearing in Sydney on 31 July 2003, the Committee was informed by Treasury of the gazettal of the Superannuation Industry (Supervision) Amendment Regulations 2003 and the Retirement Savings Accounts Amendment Regulations 2003, dated 30 July 2003. The Committee makes a comment on this gazettal in its 'Statement on the Gazettal of the Regulations' at the conclusion of this report.

Importantly, however, the Committee wishes to place on record that it interpreted its terms of reference as requiring it to inquiry into the provisions of the gazetted regulations where they differed from the draft regulations.

Oral contributions were taken from 37 witnesses or groups of witnesses. A list of witnesses is at **Appendix Two**. The Committee took 168 pages of evidence. The *Hansard* of the hearings is available at the Hansard site at www.aph.gov.au. References in this report are to the proof Hansard.

A list of tabled documents is at **Appendix Three**.

A list of previous Committee reports is at **Appendix Four**.

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PREFACE

The Superannuation Industry (Supervision) Amendment Regulations 2003 (No. 4) and the Retirement Savings Accounts Amendment Regulations 2003 (No. 2), dated 30 July 2003, are designed to extend access to portability of superannuation in Australia. Portability of superannuation is the ability of superannuation fund members to roll over/transfer existing superannuation benefits from one regulated superannuation fund, approved deposit fund or retirement savings account to another. The regulations are due to commence on 1 July 2004.

Portability of superannuation is distinct from choice of superannuation fund, which refers to the ability of employees to choose the fund to which their employer directs future superannuation guarantee contributions.

Importantly, many superannuants in Australia already have access to portability of their superannuation funds. Under the governing rules of the vast majority of Australian superannuation funds, a member can already elect to roll over/transfer his or her crystallised benefit to any other nominated superannuation fund.

During the conduct of the Committee's inquiry, the Committee received evidence on the regulations from a broad range of parties including peak industry bodies, superannuation funds or fund trustees, professional financial organisations, financial service providers, peak employee and employer groups and the relevant government agencies. In general terms, there was support for the principle of portability, but considerable opposition to the specific terms of the regulations.

The principal concern expressed by parties about the regulations was that they would mandate the right of superannuation fund members to roll over/transfer their superannuation savings out of an active fund (ie one still receiving employer sponsored superannuation guarantee contributions) into an inactive fund. It was argued that this would effectively constitute *de facto* choice of fund, or choice of fund by the back door.

In its conclusions and recommendations, the Committee supports the principle of portability, and the ability of individuals to consolidate their superannuation accounts. In particular, the Committee supports giving individuals the ability to consolidate an inactive superannuation account into either an active account or another inactive account. Such a measure, accompanied by a targeted education campaign when the portability regulations come into effect, would achieve a reduction in superannuation account numbers in Australia.

However, the Committee believes that portability out of an active superannuation account is an issue which is better dealt with through choice of funds legislation on the grounds of efficiency and consumer protection. There may also be concerns where a person's death benefit is significantly greater than the member's account balance. In addition, portability out of active superannuation accounts could lead to an increase in superannuation account numbers in Australia, rather than the desired decrease.

Accordingly, the Committee believes that the portability regulations should be revised prior to 1 July 2004, when the regulations are due to commence, to prohibit roll overs/transfers out of an active superannuation account.

The Committee also believes that a number of other improvements should be made to the portability regulations prior to 1 July 2004, including:

- Revising regulation 6.34(2) of the Superannuation Industry (Supervision) Amendment Regulations 2003 (No.4) relating to disclosure to clarify its proposed operation and to protect trustees and employers from any retrospective legal action;
- Revising regulation 6.30(2)(c) of the Superannuation Industry (Supervision) Amendment Regulations 2003 (No.4) to exclude defined benefit schemes from the provisions of the regulation where the member's current entitlement is in accumulation or partially vested form;
- Excluding Queensland Local Government Super (and any other funds in a similar position) from the operation of the Superannuation Industry (Supervision) Amendment Regulations 2003 (No.4) due to the particular nature of the scheme under state legislation;
- Including a roll over/transfer protocol, based on consultation with the industry, to help facilitate roll overs/transfers;
- Examining the timing, suspension and variation of roll overs/transfers under regulations 6.34, 6.36 and 6.37 of the Superannuation Industry (Supervision) Amendment Regulations 2003 (No.4); and
- The inclusion of a section giving specific legal protection to trustees, in accordance with a model outlined by the Law Council of Australia.

In addition, the Committee notes additional measures which could be undertaken by Government to further facilitate the introduction of portability of superannuation in Australia. In particular, the Committee believes that when the portability regulations come into effect, the Government should commence its education campaign using the $28.7 million allocated by the Government over four years in the 2002-2003 Budget.

Finally, the Committee observes that the gazetted regulations also raise a number of issues similar or identical to those relating to choice of fund legislation. In particular, the regulations raise issues in relation to guaranteeing the safety of any portability and choice system by ensuring consumers are fully informed and protected. These issues

were previously addressed by this Committee in its November 2002 report entitled *Provisions of the Superannuation Legislation Amendment (Choice of Superannuation Funds) Bill 2002*.

Senator John Watson
Committee Chair

LIST OF ABBREVIATIONS

AAS	Australian Administrative Services
ABA	Australian Bankers' Association
ABN	Australian Business Number
ACA	Australian Consumers' Association
ACTU	Australian Council of Trade Unions
ADF	Approved deposit fund
AIG	Australian Industry Group
AIST	Australian Institute of Superannuation Trustees
APRA	Australian Prudential Regulation Authority
ASFA	Association of Superannuation Funds of Australia
ASIC	Australian Securities and Investments Commission
ATO	Australian Taxation Office
Cbus	Construction and Building Unions Superannuation
CPA Australia	Certified Practicing Accountants Australia
EPSSS	Exempt public sector superannuation scheme
FPA	Financial Planning Association
FSR Act	*Financial Services Reform Act 2001*
IAA	Institute of Actuaries of Australia
IFF	Industry Funds Forum
IFFP	Industry Funds Financial Planning
IFSA	Investment and Financial Services Association
MTAA Super	Motor Trades Association of Australia Superannuation Fund

RSA	Retirement savings account
SG	Superannuation guarantee
SIS Act	*Superannuation Industry (Supervision) Act 1993*
SOS	Society of Superannuants

RECOMMENDATIONS

Recommendation 1

The Committee recommends that the Government prior to 1 July 2004 revise the Superannuation Industry (Supervision) Amendment Regulations 2003 (No. 4) and the Retirement Savings Accounts Amendment Regulations 2003 (No. 2) to prohibit roll overs/transfers out of an active superannuation account.

Recommendation 2

The Committee recommends that when revising the Superannuation Industry (Supervision) Amendment Regulations 2003 (No. 4) and the Retirement Savings Accounts Amendment Regulations 2003 (No. 2), the Government should also address the issues raised in Paragraph 12.73.

Recommendation 3

The Committee recommends that the Government prepare for the introduction of portability and choice by addressing the issues raised in paragraph 12.74. In particular, the Committee believes that when the portability regulations come into effect, the Government should commence its education campaign using the $28.7 million allocated by the Government over four years in the 2002-2003 Budget.

Chapter One

Background

Introduction

1.1 This chapter provides:

a) Background information to the regulations;

b) Information on current levels of portability in Australia;

c) An analysis of the main provisions of the draft and gazetted portability regulations; and

d) A summary of parties making submissions to the inquiry.

Background to the regulations

1.2 Treasury defines portability of superannuation as the ability of a member to roll over/transfer existing superannuation benefits from one regulated superannuation fund, approved deposit fund (ADF) or retirement savings account (RSA) to another regulated superannuation fund, ADF, RSA or exempt public sector superannuation scheme (EPSSS).[1]

1.3 This is distinct from choice of superannuation (choice), which refers to the ability of employees to choose the fund to which their employer directs future superannuation guarantee (SG) contributions. Choice of superannuation was most recently brought before the Parliament in the Superannuation Legislation Amendment (Choice of Superannuation Funds) Bill 2002.

1.4 In its 2001 pre-election statement on superannuation, *A Better Superannuation System*, the Government restated its earlier commitment to the introduction of portability of superannuation. The Government's stated position was that workers should have the freedom to decide who manages their superannuation and the right to move their benefits from one fund to another.[2]

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1 Commonwealth Treasury, *Portability of Superannuation Benefits: Enhancing the Right of Members to Move Existing Benefits Between Superannuation Entities*, Consultation Paper, September 2002, p. 5.

2 *Submission* 25, Treasury, p. 1.

1.5 In September 2002, Treasury released for comment a consultation paper on portability entitled 'Portability of Superannuation Benefits: Enhancing the Rights of Members to Move Benefits between Superannuation Entities'. In this paper, Treasury argued that portability of superannuation in Australia would have a number of benefits:

a) It would assist in addressing the issue of multiple superannuation accounts;

b) It would increase competition between superannuation funds and place pressure on funds to reduce fees and charges; and

c) It would complement the Government's choice of funds legislation. As stated in the consultation paper, choice provides employees with an opportunity to choose the fund into which their future mandated SG contributions are paid. Portability allow individuals to move existing contributions and earnings into the fund of their choice.[3]

1.6 Although not in the formal objectives stated in the Treasury consultation paper, the Committee notes that the Assistant Treasurer, Senator Coonan, has also publicly referred to the importance of consumers being able to get out of poorly performing funds. In her media release C040/03 dated 25 May 2003, Senator Coonan stated:

> Portability will allow Australians to transfer benefits from their current superannuation fund to a fund of their choice. This will allow members to consolidate their superannuation benefits into one fund if they so wish. Maintaining superannuation benefits in multiple funds can significantly erode an employee's retirement benefit and lead to lost superannuation accounts.

1.7 Following receipt of comment on the consultation paper, Treasury released draft portability regulations for public consultation on 27 May 2003. Following a further period of consultation, the Government gazetted final portability regulations on 30 July 2003. They are:

a) the Superannuation Industry (Supervision) Amendment Regulations 2003; and

b) The Retirement Savings Accounts Amendment Regulations 2003.

1.8 It is notable that while it is proposed that portability be implemented by regulation rather than an Act of Parliament, other provisions dealing with roll overs and transfers of benefits are also dealt with in regulation made under the *Superannuation Industry (Supervision) Act 1993* (SIS Act).

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3 Commonwealth Treasury, *Portability of Superannuation Benefits*, pp. 5-6.

Current portability in Australia

1.9 Both Treasury and the Australian Prudential Regulation Authority (APRA) have separately noted that current portability arrangements in Australia vary for members of Superannuation funds and ADFs on the one hand, and members of RSAs on the other. Accordingly, member access to portability in Australia at present depends on each fund's governing rules:[4]

a) Members of Superannuation funds and ADFs: There is currently no provision within the SIS Act that requires a fund to roll over/transfer existing superannuation benefits at the request of a member. By default, the ability of a member to roll over/transfer existing superannuation benefits is regulated by each individual fund's governing rules. [5]

b) Members of RSAs: Under the *Retirement Savings Accounts Act 1997*, RSA providers are required to provide portability. Under section 50 of the RSA Act, an RSA provider must, at the request of a member, roll over/transfer the requested amount as soon as practicable or, if the contract or agreement for the provision of the RSA specifies a period, within the period specified. In any case, the roll over/transfer must be made within 12 months after receipt of a written request.[6]

1.10 In its written submission, APRA made the following observations on the general availability of portability in Australia, based on its regulatory reviews and on-site visits to superannuation funds:

- Most retail funds offer roll overs/transfers but apply fee-related conditions. For example, an exit fee scale may vary according to the length of time the member has been in the fund, or an entry fee may apply.
- Few corporate funds roll over/transfer members' accumulated benefits from the fund whilst the member is still employed by the contributing employer. Cessation of employment prior to retirement will generally, under fund rules, trigger a requirement to leave the fund.
- Some industry funds will not roll over/transfer benefits whilst the member remains in the same industry, however the policy varies from fund to fund.

1.11 The Committee notes that APRA also indicated in its written submission that it collects general data on membership flows, including exits by roll overs/transfers.

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4 Commonwealth Treasury, *Portability of Superannuation Benefits*, pp. 7-8. *Submission* 14, APRA, p. 2.

5 Commonwealth Treasury, *Portability of Superannuation Benefits*, p. 7.

6 Commonwealth Treasury, *Portability of Superannuation Benefits*, pp. 7-8. *Submission* 24, Treasury, p. 1. *Submission* 14, APRA, p. 2.

During the December quarter 2002, 1.3 per cent of members of the survey fund population rolled over or transferred to another fund.[7]

1.12 In its written submission, the Investment and Financial Services Association (IISA) also made a number of observations similar to those of APRA above on the current availability of portability:

- Retail (personal) superannuation funds do not restrict the circumstances in which consumers can transfer their personal superannuation out of a fund. Customers can request part or full balance rollovers/transfers.
- Many corporate superannuation funds (funds offered by employers, as opposed to master trusts) require a SIS trigger event before making a roll over/transfer. This would usually be on leaving the employer by resignation, retirement or retrenchment.
- Defined benefit funds generally do not allow portability of superannuation benefits. Unfunded defined benefit funds routinely restrict portability of benefits, even after a member has left employment.[8]

1.13 A full copy of IFSA's submission on the current levels of portability is at **Appendix Five**.

Main provisions of the regulations

1.14 The Government's gazetted regulations are designed to extend the ability of superannuation fund members to roll over/transfer their existing superannuation benefits to another superannuation fund, ADF, RSA or exempt public sector superannuation scheme EPSSS. The major provisions of the portability regulations are examined below:

a) Application: The regulations apply to accumulation funds and members of fully funded defined benefit funds who have left employment with an employer-sponsor of the fund. They do not apply to unfunded public sector superannuation schemes, self-managed superannuation funds, or benefits being paid as a pension (other than an allocated pension).

b) Timing of roll overs/transfers: The regulations require that trustees must roll over/transfer a benefit to another fund as soon as practicable, but in any case within 90 days of the request from the member.

c) Information for members: The regulations require that, prior to making a transfer, the trustee must be satisfied that a member is aware

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7 *Submission* 14, APRA, pp. 2-3.

8 *Submission* 21, IFSA, pp. 2-3. See also *Committee Hansard*, 31 July 2003, p. 32.

of his or her right to receive additional information on the effect of the roll over/transfer (eg. impact of fees or insurance cover) or must be satisfied that the member does not require such information.

d) Protected members: The regulations require that fees charged on a protected member's account cannot exceed the interest credited to that account. Members who roll over/transfer money out of a superannuation fund will lose the right to protected member status within that fund.

e) Partial roll overs/transfers: The regulations provide that if a member of a superannuation fund wishes to make a partial roll over/transfer (less than their entire withdrawal benefit), the trustee can require the member to leave a balance of up to $5,000 behind in the fund.

f) Frequency of roll overs/transfers: The regulations provide that a trustee will only be required to affect one roll over/transfer per year for each member of a fund, though they will be free to offer more regular roll overs/transfers if they wish.

g) Role of APRA: The regulations provide APRA with the power to freeze or alter a fund's ability to provide portability if it believes there may be an adverse financial impact on the fund. Trustees will be able to apply to APRA to exercise this power.

h) Commencement: The regulations are due to commence on 1 July 2004.[9]

1.15 The full text of the regulations is at **Appendix Six**.

1.16 Significantly, the Committee notes that the regulations gazetted on 30 July 2003 contained some major revisions from the draft regulations as released on 27 May 2003, as referred to this Committee for inquiry. In particular, the gazetted regulations:

a) Introduced the new requirements in relation to information for members on the effect of a roll over/transfer (point "c" above);

b) Introduced the restriction on partial roll overs/transfers to enable trustees to require that a member retain $5,000 in an account following a roll over/transfer (point "e" above); and

c) Introduced the restriction on the frequency of roll overs/transfers to enable trustees to refuse to implement more than one roll over/transfer per year (point "f" above).

9 *Submission* 24, Treasury, p. 2.

1.17 Importantly, the Committee notes that almost all parties making submissions to this inquiry responded to the draft regulations, rather than the gazetted regulations dated 30 July 2003. In addition, some of the evidence given to the Committee during the hearing on 31 July 2003 referred specifically to the draft regulations. Where relevant, the Committee refers to this fact in this report and makes allowance for this in its conclusions and recommendations.

Parties to the inquiry

1.18 The Committee received submissions to the inquiry from a broad range of organisations including:

a) Peak industry bodies such as the Association of Superannuation Funds of Australia (ASFA), the Corporate Super Association, the Australian Institute of Superannuation Trustees (AIST), the Industry Funds Forum (IFF) and the Society of Superannuants (SOS);

b) Superannuation funds or fund trustees such as the Motor Trades Association of Australia Superannuation Fund (MTAA Super), Queensland Local Government Super, the Construction and Building Unions Superannuation (Cbus) and the Government Employees Superannuation Board of Western Australia;

c) Professional financial and legal organisations such as the Institute of Actuaries of Australia (IAA), IFSA, Certified Practicing Accountants Australia (CPA Australia), the Financial Planning Association (FPA), the Australian Bankers' Association (ABA) and the Law Council of Australia;

d) Consumer representatives such as Taxpayers Australia and the Australian Consumers' Association (ACA);

e) Financial service providers such as Mercer Human Resource Consulting, Watson Wyatt Australia, Australian Administrative Services (AAS) and Superpartners;

f) Peak employee group the Australian Council of Trade Unions (ACTU);

g) Peak employer group the Australian Industry Group (AIG);

h) The relevant government agencies APRA and the Commonwealth Treasury.

Supporters of the regulations

1.19 The Committee notes general support for the principle of portability of superannuation, on the basis that superannuation fund members have the right to manage their superannuation.

1.20 In this regard, the Committee notes that the FPA commissioned Roy Morgan to conduct research on superannuation in November 2002. A large number of respondents to the survey supported the concept of portability. For example, eight-eight per cent of people surveyed said they would like to keep their current superannuation fund if they were to change jobs.[10]

1.21 However, only IFSA, the ABA, Treasury and APRA made submissions in support of the draft or gazetted regulations. IFSA supported the regulations on the basis that they provide an important improvement in the ability of Australians to place their superannuation in a fund of their choosing. IFSA argued that currently, many Australians are not able to move their superannuation to another superannuation fund unless they satisfy a trigger event or condition of release under the SIS Act or regulations.[11] This was reiterated by Mr Gilbert from IFSA in the hearing of 31 July 2003:

> Turning to portability, we support the portability of superannuation benefits as a key consumer sovereignty issue. We stress that consumer sovereignty should be at the heart of these sorts of decisions. 'Consumer sovereignty' is a complex term and a complex concept. It includes taking into account such things as the right of consumers to select where their money should be in terms of returns, where their money should be in terms of fees and where their money should be in terms of the entity which is managing those moneys and the entities managing the moneys underneath.[12]

1.22 Similarly, the ABA, in its written submission, fully supported the regulations. The ABA indicated that the simple principle behind its position is that the best governance occurs when people are informed and freely choose which financial services provider they will trust with their funds.

1.23 The Committee also notes the evidence of Mr Murray from Treasury in the hearing on 13 August 2003 that the regulations would simply extend the availability of portability in Australia to a further group of fund members:

> Portability also already exists in many forms. Many funds already provide portability. I am certainly not aware of that causing significant problems in the industry at the moment. All that the new portability regime is really doing is extending that same right to a further group of members.[13]

Opponents of the regulations

1.24 In evidence to the Committee on 13 August 2003, Mr Riordan from the Law Council of Australia argued that the portability regulations are simply unnecessary.

10 *Submission* 24, FPA, p. 2.

11 *Submission* 21, IFSA, p. 1.

12 *Committee Hansard*, 31 July 2003, p. 27.

13 *Committee Hansard*, 13 August 2003, p. 16.

Mr Riordan argued that the vast majority of superannuation fund members in Australia can already elect to transfer crystallised benefits to another nominated fund if they so wish.[14]

1.25 However, the vast majority of parties to the inquiry, while supporting portability in principle, opposed various aspect of the regulations, or raised significant concerns about the capacity of the industry and consumers to successfully adopt portability at this time. These issues are addressed in the following chapters.

14 *Committee Hansard*, 13 August 2003, p. 1.

Chapter Two

Portability and Choice

Introduction

2.1 This chapter examines:

a) The ability of fund members under the regulations to roll over/transfer funds out of an active superannuation account, and claims that this effectively constitutes choice of superannuation by the back-door;

b) Whether the portability regulations can operate independently of choice; and

c) Arguments that the portability regulations should have been considered by Parliament concurrently with choice of fund legislation.

Roll over/transfer out of an active account

2.2 The principal concern expressed by parties in response to the draft regulations was that they would mandate the right of superannuation fund members to roll over/transfer their superannuation savings out of an active account (ie one still receiving employer sponsored SG contributions) into an inactive account.

2.3 The Committee notes that ASFA,[1] IFF,[2] AIG,[3] AAS,[4] Watson Wyatt,[5] CPA Australia,[6] the Corporate Super Association,[7] the Institute of Chartered Accountants in Australia[8] and the ACA[9] all argued this point in their written submissions. In effect, giving fund members the right to roll over/transfer funds out of an active account

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1 *Submission* 2, ASFA, p. 3.

2 *Submission* 4, IFF, p. 3.

3 *Submission* 5, AIG, p. 2

4 *Submission* 18, AAS, p. 3.

5 *Submission* 12, Watson Wyatt, p. 1.

6 *Submission* 13, CPA, p. 1.

7 *Submission* 9, Corporate Super Association, p. 4.

8 *Submission* 22, The Institute of Chartered Accountants in Australia, p. 2.

9 *Submission* 32, ACA, p. 2.

would essentially constitute *de facto* choice - introducing choice of fund under the guise of portability. The Law Council of Australia expressed the matter in this way:

> The portability regime as set out in the Draft Regulations could result in a situation where amounts are contributed by an employer one day and then moved to another superannuation fund the next. In effect, this would amount to choice of fund by the member when, as the Senate Select Committee is aware, choice of fund legislation has not been passed by Parliament.[10]

2.4 The Committee notes that similar concerns were expressed in hearings by Mr Jeffrey from Watson Wyatt,[11] Mr Watson from MTAA Super,[12] Ms Galbraith from Superpartners,[13] Ms Rubinstein from the ACTU,[14] Mr Silk from IFF,[15] Mr Riordan from the Law Council of Australia[16] and Dr Anderson from ASFA. Dr Anderson expressed the matter this way:

> Portability without choice could become a backdoor version of choice: the employer pays contributions into a fund and the employee systematically channels them into a different fund.[17]

2.5 To address their concerns that the draft portability regulations would effectively implement *de-facto* choice, parties such as Superpartners[18] and the ACTU[19] argued that the draft regulations should be amended to remove the ability of fund members to roll over/transfer funds out of an active account. Alternatively, in its written submission, SOS argued that portability should not apply where employers are continuing to contribute to an active account, unless 50 per cent of employees in the designated fund vote otherwise.[20]

2.6 The Committee notes in this regard the evidence of Mr Ward from Mercer in the hearing on 1 August 2003 that an appropriate measure of whether an account is active or inactive would be whether the fund had received any contributions in the last

10 *Submission* 20, Law Council of Australia, p. 5.

11 *Committee Hansard*, 31 July 2003, p. 35.

12 *Committee Hansard*, 31 July 2003, p. 10.

13 *Committee Hansard*, 1 August 2003, p. 16.

14 *Committee Hansard*, 1 August 2003, p. 46.

15 *Committee Hansard*, 1 August 2003, p. 2.

16 *Committee Hansard*, 13 August 2003, p. 3.

17 *Committee Hansard*, 31 July 2003, p. 14.

18 *Submission* 8, Superpartners, pp. 1-2.

19 *Submission* 10, ACTU, p. 2.

20 *Submission* 19, SOS, p. 1.

12 months. This would be sufficient time to pick up some cyclical casual jobs such as fruit picking.[21]

2.7 The Committee notes that in the gazetted regulations, the Government amended the draft regulations so that trustees will only be required to affect one roll over/transfer per year for each member of a fund, although they will be free to offer more regular roll overs/transfers if they wish.

2.8 In the Committee's hearings, a number of parties welcomed this restriction on roll overs/transfers, although they nevertheless highlighted that fund members are still allowed one transfer a year out of an active account into an inactive account, which still effectively amounts to choice of fund. For example, Mr Jeffrey from Watson Wyatt commented:

> … I think it is a sensible move. I recognise that it reduces the flexibility of choice, but you have got a tension there between full flexibility and addressing the behavioural issues you referred to before. So it sounds sensible to put on a cap of once a year. But still you have got choice. It is one year, but then every one year you roll over money. You still have fund choice, just with a slightly longer lag … [22]

2.9 Similarly, Mr Silk from IFF observed in the hearing on 1 August 2003:

> The change to a limit of one per year is an improvement, but represents an incremental improvement rather than a fundamental beneficial change to the regulations as originally proposed. That change does not address the fact that the regulations overall still represent choice of fund without the safeguards that we say should go with such a system.[23]

2.10 The Committee also note, however, the point of Mr Ward from Mercer in the hearing on 1 August 2003 that the restriction on roll overs/transfers out of an active account is welcome, but to limit roll overs/transfers out of inactive accounts, thereby effectively hampering account consolidation, is not welcome.[24]

2.11 The Committee raised this issue of portability out of active accounts with Mr Murray from Treasury in the hearing on 13 August 2003. In response, Mr Murray stated:

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21 *Committee Hansard*, 1 August 2003, p. 30.

22 *Committee Hansard*, 31 July 2003, p. 39.

23 *Committee Hansard*, 1 August 2003, p. 3.

24 *Committee Hansard*, 1 August 2003, p. 27.

> I do not think portability is choice of fund. Portability allows you to move your existing benefits from your fund, as opposed to determining where your future contributions will go.[25]

2.12 The Committee also notes the evidence of Mr Riordan of the Law Council of Australia that while many corporate funds require employer's consent before an employee can roll over/transfer the balance of a active account, many industry superannuation funds no longer place any restrictions on the roll over/transfer of member's active accounts.[26]

The independence of portability and choice?

2.13 Following on from the concerns raised above, a number of parties to the inquiry also argued that the portability regulations should not operate independently of choice legislation.

2.14 For example, ASFA argued in its written submission that the Government has directly associated portability with choice in its general policy statement, *Heading in the Right Direction – Securing Australia's Future* and its pre-election statement on superannuation, *A Better Superannuation System*. In addition, ASFA noted that the Government directly linked the twin policies in the 2002 Budget Papers. ASFA strongly supported this linkage:

> ASFA believes that where employees avail themselves of the opportunity to choose the fund into which future mandated employer contributions are to be paid, they should also be given the opportunity to move their existing benefits into that fund of choice. Portability is viewed as complementing choice, not a method of delivering choice.[27]

2.15 Similar positions were also expressed by CPA Australia,[28] IAA,[29] SOS,[30] AAS[31] and the FPA[32] in their written submissions. Indeed, Mercer argued that there are more complexities in relation to the introduction of portability than the introduction of choice, and that therefore Mercer would not be concerned if portability was introduced after choice, subject to the resolution of various practical issues.[33]

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25 *Committee Hansard*, 13 August 2003, p. 16.

26 *Committee Hansard*, 13 August 2003, p. 3.

27 *Submission* 2, ASFA, p. 3.

28 *Submission* 13, CPA, p. 1.

29 *Submission* 15, IAA, p. 5.

30 *Submission* 19, SOS, p. 1.

31 *Submission* 18, AAS, p. 1.

32 *Submission* 24, FPA, p. 3.

33 *Submission* 17, Mercer, p. 2.

2.16 The Committee notes, however, that in evidence to the Committee on 31 July 2003, Mr Gilbert from IFSA argued that portability can proceed without choice.[34]

2.17 This position was reiterated by Mr Murray from Treasury in the hearing on 13 August 2003:

> I think the government sees the portability policy as being able to stand alone and apart from the choice of fund policy. They see it as bringing in benefits on its own. It is complementary to choice—and that is correct—but it can also stand on its own.[35]

Legislative scrutiny of portability and choice

2.18 Following on from debate about the independent operation of portability and choice, a number of parties argued that the portability regulations should have been presented to the parliament for consideration concurrently with choice legislation, and not before.

2.19 For example, MTAA Super argued that there has been general speculation in the superannuation industry and at previous hearings of this Committee that portability is less controversial than choice. However, MTAA Super disputed this suggestion. MTAA Super argued that the key reason that portability has not been as keenly scrutinised and debated to date is because the majority of the industry stakeholders has always believed that choice and portability would be introduced together and could be considered concurrently.[36]

2.20 Accordingly, MTAA Super strongly advocated that the issues of portability and choice should be considered jointly by the Parliament. MTAA Super continued:

> This would allow the Parliament to better understand and judge the effectiveness of the existing options and mechanisms already available to fund members and their employer-sponsors in respect of the transfer of superannuation between funds rather than having the currently proposed choice of fund and portability prescription imposed which may overly and unnecessarily add to the already complex web of superannuation regulation in Australia.[37]

2.21 Similarly, the Corporate Super Association also suggested that, since choice of fund for prospective contributions is subject to such significant community debate,

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34 *Committee Hansard*, 31 July 2003, p. 27.

35 *Committee Hansard*, 13 August 2003, p. 15.

36 *Submission* 6, MTAA Super, p. 6.

37 *Submission* 6, MTAA Super, p. 5.

it would be an abuse of the regulation making power to introduce a broader form of choice without subjecting the proposals to full Parliamentary process.[38]

2.22 Again, the Committee notes that this evidence was strongly reiterated in hearings. For example, Mr Jeffrey from Watson Wyatt stated:

> Our overriding concern with the draft portability regulations is that they, effectively, introduce choice of fund before the primary choice of fund legislation has been passed. We believe it is inappropriate for these regulations to be passed before the choice of fund legislation is passed.[39]

2.23 Similarly, Mr Silk from IFF stated in the hearing on 2 August 2003:

> … the portability provisions and the choice of fund provisions should be considered together as part of the same package. They both relate to the circumstances in which a member can transfer their superannuation from one fund to another. It is quite absurd, in our submission, to have the regulatory provisions governing the transfer of previous contributions to be different from those governing the transfer of future contributions.[40]

2.24 Similar concerns were expressed in hearings by Mr Watson from MTAA Super,[41] Mr Korchinski from AAS,[42] Mr Hristodoulidis from the FPA,[43] Capt Woods from SOS,[44] Ms Galbraith from Superpartners,[45] Mr Ward from Mercer,[46] Mr Shallue from IAA,[47] Ms Rubinstein from the ACTU[48] and Ms Kelleher from CPA Australia.[49]

<u>Revisions to choice legislation</u>

2.25 The Committee notes that on 25 May 2003, the Assistant Treasurer, Senator Coonan, outlined in a media release amendments to the Government's choice model as proposed in the Superannuation Legislation Amendment (Choice of Superannuation Funds) Bill 2002. The Government plans to introduce revised choice legislation in the spring sittings of Parliament.

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38 *Submission* 9, Corporate Super Association, p. 4.

39 *Committee Hansard*, 31 July 2003, p. 35.

40 *Committee Hansard*, 1 August 2003, p. 2.

41 *Committee Hansard*, 31 July 2003, pp. 3-4.

42 *Committee Hansard*, 31 July 2003, p. 52.

43 *Committee Hansard*, 31 July 2003, p. 60.

44 *Committee Hansard*, 31 July 2003, p. 69.

45 *Committee Hansard*, 1 August 2003, p. 12.

46 *Committee Hansard*, 1 August 2003, p. 26.

47 *Committee Hansard*, 1 August 2003, p. 39.

48 *Committee Hansard*, 1 August 2003, p. 46.

49 *Committee Hansard*, 1 August 2003, p. 51.

2.26 The changes to the choice model, as outlined by the Assistant Treasurer in her media release on 25 May, are reproduced in Table 2.1 over. The proposed commencement date for choice remains 1 July 2004.

Table 2.1: Revisions to the Government's Choice of Funds Model

	2002 Choice Bill	**Proposed Arrangement**
Default funds	The default fund rules require an employer to go through a maximum of three steps: - If the employee is covered by an award, the default fund is a fund nominated in that award. - If an award does not exist, the default fund is the majority fund (ie. the fund that the majority of employees are members). - If there is no majority fund, the employer can choose any complying fund.	Retain the status quo. Employers will choose a complying fund into which superannuation guarantee contributions will be paid if there is no chosen fund.
Penalty provision	A maximum penalty of $6,600 per breach following ATO prosecution action.	A maximum penalty of $500 per breach. The Commissioner of Taxation has the discretion to reduce the penalty (including to nil) depending on individual circumstances.
Employee information	Employers can request account information from the employee about a chosen fund.	Employers do not have to accept a chosen fund if the employee does not provide relevant account information.
Choice process	Employee can choose a fund under a formal process - employer must provide a standard choice form within 28 days; - employees have 28 days to choose a fund. Employee can have an individual written agreement (where employer has discretion to reject the choice).	Only one process. Employer required to provide a standard choice form before 29 July 2004 for existing employees and within 28 days of when the employee commences employment, or on request. 28 day restriction on choosing a fund has been deleted. Employee can choose a fund at any time provided they have not exercised choice in the previous 12 months.

Chapter Three

The Impact of the Regulations on Account Numbers

Introduction

3.1 This chapter examines the likely impact of the portability regulations on superannuation account numbers, with reference to:

a) Current superannuation account numbers in Australia;

b) Claims that the regulations will lead to a proliferation of accounts; and

c) The impact of the regulations on lost account numbers.

Current superannuation account numbers in Australia

3.2 The Committee notes evidence from APRA's *Superannuation Trends* for the March quarter 2003 that the total number of superannuation accounts in Australia reached 25.5 million in the March quarter – an average of 2.8 accounts for each of Australia's 9 million fund members.

3.3 During the inquiry, a number of reasons were raised for the current proliferation of superannuation accounts in Australia:

a) Changing employment patterns: In its written submission, the FPA noted that some people have a number of jobs, with each employer paying superannuation into a different account.[1] Similarly, AIST attributed multiple accounts to the increase in job mobility and the rise of casual and part-time employment.[2]

b) A general lack of information and inertia regarding consolidation of accounts: In its written submission, ASFA argued that the large number of accounts in Australia is largely the result of failure or inability to consolidate accounts once individuals have left one employment situation and commenced another.[3] The FPA also noted

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1 *Submission* 24, FPA, p. 2.

2 *Submission* 11, AIST, pp. 1-2.

3 *Submission* 2, ASFA, p. 2.

that many people change employers without consolidating their superannuation account, by choice or inadvertently.[4]

c) Deliberate individual decisions to diversify investments across a number of providers: In its written submission, ASFA acknowledged that for some consumers, the decision to retain more than one account may be a deliberate and informed decision.[5]

d) Deliberate obstruction by funds: In the hearing on 31 July 2003, Mr Watson from MTAA Super noted that there is some evidence that some funds will deliberately frustrate a member's attempt to roll over/transfer a benefit from one fund to another.[6] The Committee received a written submission from Mr Sowton, writing in a private capacity, which provided a graphic example of deliberate obstruction by a fund of a roll over.[7]

e) The imposition of excessive exit fees and penalties on members if they seek to roll over/transfer out of a fund. In evidence to the Committee on 1 August 2003, Mr Silk from IFF argued that one of the largest inhibitors to account consolidation at the moment is the excessive exit fees and penalties that are charged by some superannuation fund providers.[8]

A proliferation of accounts?

3.4 As indicated in Chapter One, one of the principal arguments made by Treasury in its September 2002 consultation paper in favour of portability was that it would assist in addressing the issue of multiple superannuation accounts in Australia. This argument was also made by Taxpayers Australia in its written submission:

> Portability will assist in reducing the number of accounts each person holds and the resulting consolidation will improve the long-term growth of their total retirement savings.[9]

3.5 The Committee also notes the evidence of the ABA in its written submission that consolidation of many accounts into one or a few may also lead to lower fees and

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4 *Submission* 24, FPA, p. 2.

5 *Submission* 2, ASFA, p. 2.

6 *Committee Hansard*, 31 July 2003, p. 3.

7 *Submission* 30, Mr Sowton, pp. 1-3.

8 *Committee Hansard*, 1 August 2003, p. 3.

9 *Submission* 23, Taxpayers Australia, p. 2.

charges as the cost of some fees – such as certain account keeping fees and fund managers' margins – can fall as the minimum account balance rises.[10]

3.6 However, a large number of parties to the inquiry argued that far from leading to a reduction in superannuation accounts, the draft portability regulations will lead to a further proliferation of accounts. This is because of the ability of fund members under the regulations to roll over/transfer funds out of an active superannuation account into another fund, while continuing to receive employer contributions into the active account.

3.7 For example, MTAA Super argued that the draft regulations, if introduced in isolation from choice of funds, would create a 'disconnection' between the fund to which SG payments are directed by an employer and the fund which the employee considers to be his or her active or primary account – which can be an entirely different account.[11] This was reiterated by Mr Watson from MTAA Super in the hearing on 31 July 2003:

> In our view … portability without the complementary choice of fund arrangements – suitably amended in our view to more particularly consider consumer protection and other safeguards as we have previously well documented – has a real potential to lead to a proliferation of inactive accounts, which is quite the opposite to the intention of the regulations.[12]

3.8 Similarly, Superpartners argued that were the draft regulations to be implemented unchanged, funds would be faced with the prospect of members for whom employer contributions were continuing to be made requesting that their benefits be rolled over to another fund every ninety days, with associated administrative and insurance costs.[13]

3.9 This point was also made by IFF it its written submission. The IFF argued that if members of funds were free to move moneys from active superannuation accounts at any time, as appeared to be contemplated by the draft regulations, the effect would be a *proliferation* of superannuation accounts – precisely the opposite outcome to the stated objective.[14]

3.10 ASFA[15], AIST[16], Cbus, AAS[17] and the ACA[18] also highlighted this issue in their written submissions. Watson Wyatt also cited overseas experience suggesting that portability will lead to churning.[19]

10 *Submission* 29, ABA, p. 2.

11 *Submission* 6, MTAA Super, p. 3.

12 *Committee Hansard*, 31 July 2003, p. 3.

13 *Submission* 8, Superpartners, pp. 1-2.

14 *Submission* 3, IFF, p. 1.

15 *Submission* 2, ASFA, p. 3.

3.11 As indicated, these argument were raised in relation to the draft regulations. As previously noted, the gazetted regulations partially address this concern by restricting roll overs/transfers out of any account, active or inactive, to one a year.

3.12 Despite this restriction in the gazetted regulations, a number of parties in hearings nevertheless still raised their concerns in relation to a proliferation of accounts. For example, Mr Riordan from the Law Council of Australia argued in the hearing on 13 August 2003 that the gazetted regulations effectively mean more accounts, not fewer. Mr Riordan continued:

> There are two reasons for that—and we respectfully agree with your view—firstly, it does not compel the employer to follow the member with the employer's future SG contributions. The employer will do what it believes is in its interests, and that is entirely justifiable in terms of cost and administration to the fund. Secondly, a member who elects to take a transfer does not have to take all of their benefit; they can leave some behind and make partial transfers.[20]

3.13 Similar observations was made by Ms Galbraith from Superpartners,[21] Mr Ward from Mercer[22] and Mr Silk from IFF.[23]

3.14 In response to this concern that the regulations may lead to a proliferation of accounts, Mr Murray from Treasury argued that the regulations overcome specific fund rules that presently prevent some fund members from consolidating accounts. Whether account numbers actually go up or down will depend on individual fund member's decisions.

3.15 Mr Murray acknowledged that individuals may indeed choose to diversify their accounts under the regulations, thus creating more accounts. However, he also argued that individuals may choose to consolidate their inactive accounts into their active account, or to consolidate one inactive account into another inactive account.[24]

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16 *Submission* 11, AIST, p. 2.

17 *Submission* 18, AAS, p. 4.

18 *Submission* 32, ACA, p. 1.

19 *Submission* 12, Watson Wyatt, p. 3.

20 *Committee Hansard*, 13 August 2003, pp. 4-5.

21 *Committee Hansard*, 1 August 2003, p. 12.

22 *Committee Hansard*, 1 August 2003, p. 26.

23 *Committee Hansard*, 1 August 2003, p. 3.

24 *Committee Hansard*, 13 August 2003, p. 20.

Lost accounts

3.16 As indicated in Chapter One, Treasury also argued in its September 2002 consultation paper on portability that portability would assist in addressing the issue of lost superannuation accounts. Currently, there are approximately 4½ million accounts on the Australian Taxation Office (ATO) register. The definition of a lost account is two years without contributions being received by the fund, or two returned pieces of unclaimed mail.[25]

3.17 In its written submission, AAS disagreed with the contention that the draft regulations would influence the issue of lost superannuation accounts. AAS argued that fund members tend to have multiple funds because they do not take advantage of existing facilities to roll over/transfer benefits rather than because of a lack of portability.[26]

3.18 Similarly, in hearings on 31 July 2003, Dr Anderson from ASFA disputed the claim that portability would help address the large number of inactive or lost accounts.[27]

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25 *Committee Hansard*, 13 August 2003, p. 10.

26 *Submission* 18, AAS, pp. 4-5.

27 *Committee Hansard*, 14 July 2003, p. 14.

Chapter Four

Disclosure and Education

Introduction

4.1 This chapter examines:

a) Financial disclosure standards in Australia, with particular reference to the *Financial Services Reform Act 2001* (FSR Act), product disclosure statements and regulation 6.34(3) of the Superannuation Industry (Supervision) Amendment Regulations 2003; and

b) Financial education standards in Australia.

Financial disclosure standards in Australia

Financial Services Reform Act 2001

4.2 It its September 2002 consultation paper, Treasury noted that portability must be accompanied by an appropriate product disclosure and consumer protection regime. Treasury acknowledged that members must be able to make informed decisions and compare alternative superannuation products.

4.3 Disclosure requirements for superannuation funds are now provided under the Corporations Act, as amended by the FSR Act, which commenced on 11 March 2002 (subject to certain transitional arrangements). The disclosure obligations include a requirement that fund trustees provide members with certain information after each reporting period (usually 12 months). That includes amongst other things:

a) The amount of the member's withdrawal benefit at the start of the reporting period, the amount of the member's withdrawal benefit at the end of the reporting period, the method by which that amount was worked out, and the proportion of that benefit that must be preserved;

b) The amount payable on the member's death and details of any disability benefits;

c) A description of the fund's investment strategy and investment objectives;

d) A statement of fund assets and information on the fund's rate of net earnings; and

e) Information relating to the fees, charges, expenses and administrative or other operational costs of the fund and the amount of fees and charges deducted by the fund from any account held in respect of the member.[1]

4.4 The issue of disclosure and the FSR Act was raised by a number of parties in their written submissions. For example, Mercer suggested that with the FSR Act disclosure requirements only coming into force in March 2004, more time needs to be allowed to gauge the effectiveness of that legislation before the introduction of portability.[2] This was reiterated by MTAA Super,[3] SOS[4] and the ACA. The ACA stated:

> Much has been made of the capacity of the Financial Services Reform Act 2001 to lift standards in the financial services industry, by requiring enhanced training and qualification, better disclosure and improved consumer protection processes. However, many of these reforms are still untested, and while ACA hopes they will live up to the overall promise of the legislation to promote 'informed and confident decision-making' by Australian consumers, evaluation of the efficacy of these measures must be undertaken before the introduction of further sweeping changes, such as superannuation choice or portability.[5]

4.5 The Committee notes that similar concerns were also expressed in hearings by Mr Ward from Mercer[6] and Mr Shallue from IAA.[7]

4.6 In response to these concerns, IFSA argued in its written submission that the FSR Act reforms will achieve effective disclosure, reinforcing in turn consumer sovereignty.[8] This was reiterated by Mr Gilbert from IFSA in evidence on 31 July 2003:

> We have just passed perhaps the most impressive and far-reaching disclosure regime … and we should have faith in that regime.[9]

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1 Commonwealth Treasury, *Portability of Superannuation Benefits*, pp. 18-19.

2 *Submission* 17, Mercer, pp. 2-3.

3 *Submission* 6, MTAA Super, p. 5.

4 *Submission* 19, SOS, p. 2.

5 *Submission* 32, ACA, p. 3.

6 *Committee Hansard*, 1 August 2003, p. 26.

7 *Committee Hansard*, 1 August 2003, p. 39.

8 *Submission* 21, IFSA, pp. 1-2.

9 *Committee Hansard*, 31 July 2003, p. 31.

4.7 Similarly, Mr Hristodoulidis from the FPA argued in evidence on 31 July 2003 that the FSR Act provides the world's best consumer protection, and that it should be given an 'opportunity to bite'.[10]

Product Disclosure Statements

4.8 In its written submission, IFF recommended that in addition to the FSR Act reforms, portability needs to be accompanied by a number of other member safeguards. For example:

a) fee disclosure should be in dollar terms as well as in formulaic terms, and should include a 'whole of working life' figure; and

b) the assumed account balance should reflect the long-term savings nature of superannuation and should be based on a substantial sum, eg $100,000.

4.9 AIST also argued in its written submission that portability should be accompanied by greater consumer protection, including requiring all fees and charges of the relevant funds to be set out in dollar terms in writing.[11] This was reiterated by Ms Ryan from AIST in the hearing on 31 July 2003:

> We believe that the cost of moving your money around, with exit fees in particular, needs to be very well disclosed in very accessible terms so that members know when they join a fund exactly how much it will cost them should they wish to move money out of that fund. That is not the case as we speak.[12]

4.10 Given these concerns, the Committee notes that on 5 August 2003, the Australian Securities and Investments Commission (ASIC) released its new good practice model for fee disclosure in the Product Disclosure Statements of investment products. The development of this model followed the release in September 2002 of Professor Ramsay's report *Disclosure of Fees and Charges in Managed Funds*, which was commissioned by ASIC.

4.11 The new model is designed to give investors access to clear, concise and comprehensive information about the fees they will pay for an investment product. The model aims to address issues identified in Professor Ramsay's report as requiring attention, including:

- The use of common terms;
- Standardised descriptions;

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10 *Committee Hansard*, 31 July 2003, p. 61.

11 *Submission* 11, AIST, p. 2.

12 *Committee Hansard*, 31 July 2003, p. 19.

- Disclosure of the purpose of particular fees;
- Improved disclosure of adviser remuneration; and
- Transparency of fees.[13]

4.12 The Committee notes, however, concerns expressed by ASFA and others that fees can still be shown either in percentage or dollar terms, and in pre-tax or after-tax form. In addition, disclosure of so-called 'soft-dollar perks' remains difficult.

4.13 The Committee also notes a report in the *Australian Financial Review* dated 6 August 2003 in which Professor Ramsay indicated that the new fee disclosure model still leaves two issues outstanding for further development down the track:

> a) The disclosure of fees and charges in superannuation fund member statements (as opposed to prospectuses or product disclosure statements); and
>
> b) The impact that fees and charges will have on the future returns of a fund, based on appropriate and clear disclosure of assumptions.[14]

4.14 In its written submission, the ACA acknowledged that the recently-released ASIC fee template is a good first step in the disclosure of fees and charges, but that much more needs to be done before consumers could reasonably be expected to understand fees and charges across different products, and exercise portability and choice to their advantage.[15]

<u>Regulation 6.34(2) disclosure</u>

4.15 The Committee notes that in the <u>gazetted</u> Superannuation Industry (Supervision) Amendment Regulations 2003, the Government included regulation 6.34(3) which states:

> Before a trustee or a regulated superannuation fund or an approved deposit fund rolls over or transfers the amount, the trustee must be satisfied that the member:
>
> a) is aware that the member may ask the trustee for information that the member reasonably requires for the purpose of understanding any benefit entitlements that the member may have, including
>
> i) information about any fees or charges that may apply to the proposed roll over/transfer; and

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13 ASIC Media Release, 'ASIC Releases Fee Disclosure Model', 5 August 2003.

14 Australian Financial Review, 'More needs to be done: Ramsay', 6 August 2003, p. 45.

15 *Submission* 32, ACA, p. 3.

ii) information about the effect of the proposed roll over/transfer on any benefit entitlements the member may have; and

b) does not require such information.

4.16 In evidence to the Committee on 1 August 2003, Ms Rubinstein from the ACTU argued that this new regulation does not go any way towards the kind of disclosure and information required.[16]

4.17 In addition, Ms Galbraith from Superpartners expressed concern that it is unclear how this mechanism is meant to work, and that it may potentially become a 'rubber stamp exercise'.[17] This concern was also expressed by Mr Ward from Mercer:

> We have not had long to analyse those—and I have not had a chance to discuss it with my colleagues—but I find it very unclear what those requirements impose on trustees. I think those rules would certainly need to be clarified.[18]

4.18 The Committee also notes the evidence of Mr Shallue from IAA on 1 August 2003. Mr Shallue raised concern whether there is sufficient protection for trustees and employers against the possibility that a member makes a poor investment decision, and later tries to sue the employer or trustee for allowing them to make that poor decision. In particular, Mr Shallue argued that regulation 6.34(2) is very much open to interpretation.[19] This concern was also raised by Ms Kelleher from CPA Australia.[20]

Financial education standards in Australia

4.19 In addition to concerns in relation to financial disclosure standards, various parties to the inquiry submitted that individual employees in Australia lack the financial education necessary to make informed decisions about portability of superannuation.

4.20 In its written submission, CPA Australia highlighted that information from CPA's membership indicates that the level of superannuation awareness and understanding amongst CPA clients is in the extremely poor to poor categories. CPA attributed this largely to the complexity of Australia's superannuation system and the perception that the superannuation rules and regulations are subject to continual change. Accordingly, CPA argued that portability, with or without choice, will only be

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16 *Committee Hansard*, 1 August 2003, p. 47.

17 *Committee Hansard*, 1 August 2003, p. 14.

18 *Committee Hansard*, 1 August 2003, p. 27.

19 *Committee Hansard*, 1 August 2003, p. 43.

20 *Committee Hansard*, 1 August 2003, p. 52.

effective if it is supported by a comprehensive government funded education program.[21]

4.21 Similarly, in its written submission, AAS noted ongoing concerns that there is a general lack of financial literacy in the community, particularly in relation to superannuation. AAS suggested that this problem is exacerbated by the large number of young superannuation fund members who see superannuation only as an issue for many years in the future.[22] Similar positions were expressed by Cbus[23] and ASFA in their written submissions.[24]

4.22 In addition, concerns regarding the financial literacy of Australians, especially as regards superannuation, were also raised in hearings. For example, Mr Watson from MTAA Super stated:

> … I do not subscribe to the view that we can throw a lot of money at the tax office and have an informed education campaign which in six or 12 months will improve that. The education campaign that has to occur in terms of superannuation and retirement savings is generational – it is going to take that long – but we have to start somewhere. … I think it needs to be in the curriculum in schools, it needs to be taught in universities, it needs to be taught in the workplace, it needs to be done by funds and it needs to be done by government.[25]

4.23 Similar concerns were expressed by Mr Silk from IFF[26] and Ms Galbraith from Superparners.[27] Ms Galbraith also highlighted the findings of the recent ANZ financial literacy survey[28] which found that while investment fundamentals are well understood, with 85 per cent of people knowing that high returns equal high risk, nevertheless investors are potentially susceptible to misleading claims, with 47 per cent indicating that they would invest for 'well above market rates and no risk'. Furthermore, the ANZ survey found that of those surveyed:

- 55 per cent had little understanding of fees;
- Only 54 per cent understood that superannuation had concessional tax treatment;
- Only 25 per cent really understood compound interest;

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21 *Submission* 13, CPA, p. 1.

22 *Submission* 18, AAS, p. 5.

23 *Submission* 16, Cbus, p. 3

24 *Submission* 2, ASFA, pp. 3-4.

25 *Committee Hansard*, 31 July 2003, p. 11.

26 *Committee Hansard*, 1 August 2003, p. 2.

27 *Committee Hansard*, 1 August 2003, p. 17.

28 See ANZ Media Release, 'ANZ Releases Australia's First Financial Literacy Survey', 2 May 2003.

- 32 per cent thought that a bank account was a suitable investment for retirement; and
- Only 19 per cent could name a single disadvantage of having a managed fund, such as a decline in value of the fund.[29]

4.24 The Committee notes that in its written submission, the FPA indicated that it is a strong advocate of Government, regulators and the industry continuing to educate consumers about superannuation. It noted that it produces a publication 'Don't Kiss your Money Goodbye' in conjunction with ASIC, and proposed the development of a new publication, 'Don't Kiss your Super Money Goodbye'.[30]

An education campaign

4.25 In its September 2002 consultation paper, Treasury indicated that it would conduct an education campaign prior to the commencement of portability. The campaign would be designed to meet the information needs of both fund trustees and fund members.[31]

4.26 The need for an education campaign on portability was raised by various parties to the inquiry. For example, the ACA argued that more funding needs to be allocated to superannuation education.[32] The AIG restated its position on education from its August 2002 submission on choice:

> … there is an important need for the provision of a comprehensive and effective education campaign by the Federal Government, together with greater transparency, simplicity and consistency in prospectus material and issues such as fees and investment performance (both historical and projected). Irrespective of how portability and choice of fund are ultimately structured, the fundamental requirement for informed choice of fund selection (original and transfer via portability) remains.[33]

4.27 Similarly, in its written submission, SOS argued that the draft regulations should prescribe how education measures will be delivered and paid for. SOS also suggested that all funds be provided with Government assistance to educate their members, based on a flat dollar per head amount.[34]

4.28 The Committee notes that there is no prescription of how education measures will be delivered and paid for in the gazetted regulations.

29 *Committee Hansard*, 1 August 2003, p. 14.

30 *Submission* 24, FPA, p. 3.

31 Commonwealth Treasury, *Portability of Superannuation Benefits*, p. 21.

32 *Submission* 32, ACA, p. 3.

33 *Submission* 5, AIG, p. 2.

34 *Submission* 19, SOS, p. 2.

4.29 The Committee notes that similar matters were raised in hearings. Ms Kelleher from CPA Australia argued in the hearing on 1 August 2003 that portability and choice should be implemented only after there has been an adequate member education program undertaken by Government.[35]

4.30 The Committee also notes that in the hearing on 31 July 2003, Capt. Woods from SOS specifically raised whether the Government should be prepared to assist funds in providing education assistance to their members by providing them with financial assistance.[36]

4.31 In the hearing on 13 August 2003, the Committee raised the delivery of an education campaign on portability, and whether the $28.7 million allocated by the Government over four years in the 2002-2003 Budget applied specifically to choice, or to both choice and portability.

4.32 In reply, Treasury indicated in its response to questions on notice dated 18 August 2003 that the education campaign would target both choice of fund and portability. An extract from the 2002/03 Budget Paper No 2 states:

> The Government has allocated $28.7 million for the Australian Taxation Office to administer choice of superannuation and undertake an extensive community education campaign to inform employees and employers of their rights and obligations in relation to choice of superannuation; and inform superannuation funds and their members about portability of existing superannuation balances. The Government will give employees the choice to determine the superannuation fund into which their Superannuation Guarantee contributions are paid, and allow members of accumulation funds to move existing benefits to their fund of choice.
>
> These policies will increase competition, efficiency and performance within the superannuation industry and benefit members through lower fees and charges and increased returns.
>
> This measure will involve expenditure of $12.7 million in 2002-03, $10.3 million in 2003-04, $3.4 million in 2004-05 and $2.3 million in 2005-06 which is being fully absorbed within the existing resourcing of the ATO.[37]

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35 *Committee Hansard*, 1 August 2003, p. 51.

36 *Committee Hansard*, 31 July 2003, p. 67.

37 Cited in Treasury, Response to Questions on Notice, 18 August 2003, p. 3.

Chapter Five

Life Insurance and the Superannuation Surcharge

Introduction

5.1 This chapter examines the impact of the portability regulations on:

a) Life insurance arrangements offered by superannuation funds; and

b) Reporting and administration of the superannuation surcharge.

Life insurance arrangements

5.2 The Committee notes that many superannuation funds offer their members death and disability insurance coverage through group life insurance policies. Such policies offer fund members access to cheaper insurance cover than is available on an individual basis.

5.3 For example, in its written submission, Cbus indicated that its members have access to death and total and permanent disability insurance cover. Members may choose between 1 and 10 units of cover, with 1 unit being compulsory. In addition, employer-sponsored members in Cbus are able to access up to 4 units of insurance, without the need to undertake a medical examination.

5.4 However, during the inquiry, many parties expressed concern about the impact of the portability regulations on group life insurance policies.

5.5 For example, Cbus argued that group life insurance arrangements could be withdrawn due to the fear that members may actively select funds according to their insurance coverage. If that were to occur, Cbus noted that all superannuation fund members would be affected, even if they did not wish to exercise portability. To access coverage, members of a fund would need to provide medical information and undergo a medical test, leading to increased costs to the insurer and in turn the fund.

5.6 Cbus also noted that current automatic insurance arrangements give employees who suffer ailments such as asthma or diabetes access to affordable coverage. However, Cbus suggested that such employees could be either denied insurance cover under a portability regime, or required to pay loadings or have exclusions placed on their coverage.[1]

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1 *Submission* 16, Cbus, p. 1.

5.7 These concerns were also raised by the Law Council of Australia,[2] Mercer,[3] and AAS in their written submissions. AAS reiterated that the life insurance arrangements of many superannuation funds may be undermined by portability, which could result in:

- Members paying higher premiums;
- Some members being required to take medical examinations;
- Some members being declined insurance or only able to obtain limited insurance; and
- Restrictions on, or even the loss of, other member benefits such as the 'continuation option' which allows a member to obtain some insurance cover after leaving the service of their employer, without the need to provide any medical evidence.[4]

5.8 The Committee notes that these issues were also raised in hearings. For example, Mr Watson from MTAA Super argued in the hearing on 31 July 2003 that MTAA Super has, by independent analysis, one of the most cost-effective group life insurance policies being offered by any fund. However, under a portability regime with churning of membership of up to 25 per cent in any given contract period, Mr Watson argued that MTAA Super's insurer would insist on a complete re-rating of the costs.[5]

5.9 Similar concerns were expressed by Mr Shallue from IAA[6] and Mr Noble from Cbus, who argued that:

> … the introduction of the portability regime, as it would stand, would threaten the ability of a fund, such as Cbus, to offer a group life scheme.[7]

5.10 The Committee also notes the evidence of Mr Korchinski from AAS in the hearing on 31 July that fund members may simply forget that they have access to insurance under their superannuation scheme, and be disadvantaged as a result:

> a more significant issue is where, through ignorance, [a fund member] may transfer an amount or the majority of an amount and it does not leave enough in their previous fund to pay for insurance cover. If they move to a fund without cover, thinking that they did have cover in the new fund, and all of a sudden find that they did not have cover in the previous fund either,

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2 *Submission* 20, Law Council of Australia, p. 4.

3 *Submission* 17, Mercer, p. 5.

4 *Submission* 18, AAS, p. 9

5 *Committee Hansard*, 31 July 2003, p. 7.

6 *Committee Hansard*, 1 August 2003, p. 40.

7 *Committee Hansard* 1 August 2003, p. 21.

> then we have a consumer, a member, without insurance protection whatsoever.[8]

5.11 The Committee notes that the gazetted regulations introduce a provision allowing trustees to require members to leave a balance of up to $5,000 behind in a fund. In the hearing on 1 August 2003, Mr Ward from Mercer noted that this requirement effectively solves the concern that individuals would not have sufficient funds in their superannuation account to maintain their insurance coverage.[9] This was reiterated by Mr Murray from Treasury in the hearing on 13 August 2003.[10]

5.12 However, in the hearing on 13 August 2003, Mr Riordan from the Law Council of Australia raised concerns that trustees will nevertheless be exposed to liability for failure to inform members about risks associated with rolling over/transferring their benefits. Accordingly, Mr Riordan recommended that consideration be given to protective provisions for trustees in these circumstances.[11]

The superannuation surcharge

5.13 The Committee notes evidence in the hearing on 1 August 2003 from Mr Jeffrey of Watson Wyatt[12] and from Mr Ward of Mercer that superannuation administrators have already faced enormous difficulties in administering the superannuation surcharge. As stated by Mr Ward:

> I would also like to say a few things about the 'S' word—surcharge. Surcharge is a concept that I would say is totally alien to the superannuation environment. The legislation uses words that have never been used in a superannuation context before. It is like hammering a round peg into a square hole. There are cracks all through the peg. There are gaps down the sides and it has really only worked to the extent that it has because of a huge amount of effort put in by the tax office and a huge amount of effort put in by funds and their advisers to try to come up with a system that barely copes with the requirements. It is staggering along. When portability is introduced, the problems are magnified considerably.[13]

5.14 Reflecting Mr Ward's evidence, the Committee notes that during the inquiry, significant additional concerns were expressed in relation to the likely added impact of the portability regulations on the administration of the superannuation surcharge. In its written submission, Mercer highlighted two difficulties in particular arising from the introduction of portability under the regulations:

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8 *Committee Hansard*, 31 July 2003, p. 54.

9 *Committee Hansard*, 1 August 2003, p. 27.

10 *Committee Hansard*, 13 August 2003, p. 19.

11 *Committee Hansard*, 13 August 2003, p. 2.

12 *Committee Hansard*, 31 July 2003, p. 40.

13 *Committee Hansard*, 1 August 2003, p. 28.

a) Determining how much of a rolled over/transferred amount relates to surchargeable contributions for the current year; and

b) Handling surcharge assessments.

5.15 These issues are addressed below.

Determining surchargeable contributions for the current year

5.16 In its written submission, Watson Wyatt argued that under the portability regulations, if a partial roll over/transfer is made from a fund, the portion of the member's surchargeable contribution attributable to that roll over/transfer may not be clear, meaning that the fund may retain excessive or not retain sufficient surchargeable contributions when a surcharge assessment is received.[14] The was reiterated by Mr Jeffrey from Watson Wyatt in the hearing on 31 July 2003:

> If a partial withdrawal is taken and we have to report surchargeable contributions, a difficulty will be how much of the surchargeable contributions for that year relate to the partial withdrawal. The partial withdrawal could be in relation to a number of years of benefits. So there will need to be some way of apportioning surcharge contributions or determining whether they should be reported as moneys that have been transferred to another fund.[15]

5.17 In its written submission, Mercer argued that to cover such a contingency, industry protocols will need to be developed covering the surchargeable contributions for roll overs/transfers so that a standard practice applies. Preferably, the surcharge legislation/regulations should be amended to clearly set out the process.

5.18 Mercer further suggested that while this may seem like a minor point, from the perspective of those involved in the administration of the surcharge system, it is a major concern and the issue needs to be resolved at least 12 months before portability is introduced, in order to give funds the time to modify systems and procedures.

5.19 These points were also made by IAA in its written submission. IAA suggested that systems have been developed (with some difficulty) to cope with current surcharge reporting requirements. However, the IAA suggested that existing systems would need to be modified in order to cope with the reporting of contributions in a year in which a member makes a roll over/transfer, but continues to contribute to their old fund. IAA also recommended that should such changes to the surcharge legislation be needed, the industry should be given a further 12 months after those changes before portability is introduced.[16]

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14 *Submission* 12, Watson Wyatt, pp. 2-3.

15 *Committee Hansard*, 31 July 2003, p. 37.

16 *Submission* 15, IAA, p. 4.

5.20 Given these concerns, the Committee notes the evidence from Mr Holland of AAS in the hearing on 31 July 2003 that the restriction on roll overs/transfers to allow a trustee to require a member to leave a balance of up to $5,000 behind in the fund will go a long way to addressing the surcharge problem. At the same time, however, Mr Fitzpatrick from AAS argued:

> It will help dissipate [the surcharge problem], but I think there would still be some issues. The pushing of money around the system that we already see—where the liability for surcharge on contributions is progressively passed on to different administrators—I think potentially will be exacerbated, because there will be more pushing of contributions around as there are partial payments pushed through the system.[17]

Handling surcharge assessments

5.21 In its written submission, Mercer noted that currently when a member leaves a fund, the member's total benefit is normally paid in cash (if the relevant requirements are met) or rolled over/transferred to another fund. Thus when a surcharge assessment is received by the fund for the exited member, there are normally no remaining assets for the member, it is clear that the surchargeable contributions have been rolled over/transferred elsewhere, and the ATO is advised accordingly.

5.22 However, Mercer noted that under a portability regime, there may be many occasions where part of the benefit is retained. Even where the whole withdrawal benefit is rolled over/transferred, further contributions may be received and by the time the next surcharge assessment is received there will again be a benefit in the fund. This benefit may or may not be large enough to meet the surcharge assessment.

5.23 Mercer submitted that in such instances, there are likely to be considerable arguments as to whether the fund is still 'the holder of the contributions' as the surcharge assessment may relate to contributions made in an earlier year which have already been paid out of the fund. In such a case, the fund is no longer the holder of the contributions and should not be liable to meet the assessment.

5.24 These concerns were reiterated by Mr Ward from Mercer in the hearing on 1 August 2003:

> If, when a member leaves the employer, the whole benefit is transferred to another superannuation fund then it is fairly obvious that the new fund has become the holder of the contributions. But if we are transferring half of the member's benefit, which fund is the holder of the contributions that related to the surcharge assessment? Did the fund pay out the contributions it received 10 years ago or is it paying out the contributions it received this year or last year? There is no tying the legislation requirements for surcharge to what is actually being paid out here. How you would actually do that legislatively I have got no idea, it is just too complex. But we need

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17 *Committee Hansard*, 31 July 2003, p. 53.

> some sort of protocol established so that funds know there at least is a standard that we can all follow that asks, 'If you've transferred half your benefit, is that the first half of the contributions or the second half? Which year's contribution is it?' There is a lot of work involved in establishing that protocol. It is not going to be easy, but it needs to be done if surcharge is going to work at all. If it is not done we are going to have arguments between funds and we are going to have arguments between funds and the tax office.[18]

5.25 Once again, Mercer argued that amendments should be made to the surcharge legislation and procedures, as well as significant changes to funds' administrative systems to meet this difficulty, and that a period of at least 12 months would be necessary for the industry to amend administrative systems to cope with such a change.[19]

5.26 IAA also argued in its written submission that the reporting of surchargeable contributions and the receipt, analysis and payment of surcharge assessments is already complex, but that such complexities are only further magnified when benefits are rolled over/transferred.[20]

5.27 In the hearing on 31 July 2003, the Committee Chair raised with Mr Korchinski from AAS whether a fund, on receipt of a surcharge assessment from the ATO, would be obliged to notify a fund member that he or she could not roll over/transfer all his or her money out of the fund, due to an obligation to meet the surcharge. In response, Mr Korchinski argued that possibly a trustee could make that decision. Alternatively, Mr Korchinski suggested there would have to be rules that would apportion the payment or the balance between the various funds, but that this would be a costly and cumbersome complexity.[21]

Consultation with the ATO

5.28 Given the concern regarding the impact of the portability regulations on handling surcharge assessment, the Committee requested that officers of the ATO provide the Committee with evidence on this matter during the hearing on 13 August 2003.

5.29 In his evidence to the Committee, Mr Jackson from the ATO indicated that the process of handling surcharge assessments is based on a process beginning in around October each year with notification of member contributions from a fund, through to issuing of assessment in around May. Difficulties occur where a roll over/transfer between funds occurs in that intervening period, and the ATO effectively

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18 *Committee Hansard*, 1 August 2003, p. 29.

19 *Submission* 17, Mercer, pp. 6-7.

20 *Submission* 15, IAA, p. 4.

21 *Committee Hansard*, 31 July 2003, p. 54.

sends a surcharge assessment notice to the wrong fund. In that case, the original fund informs the ATO of the roll over/transfer, and a new assessment is issued.

5.30 In regard to an industry protocol to assist funds with handling surcharge assessments, Mr Casey from the ATO indicated that the ATO has developed a Super EC project which has been running for a little over two years which is designed to set up standard protocols for the transfer of information between funds. Most of the larger funds and administrators are already part of the Super EC group.

5.31 Given this evidence, Mr Jackson from the ATO submitted that:

> … we cannot see any difference as a result of this change in the regulations. The only difference that I guess a number of people have observed is that there may be a more frequent movement between funds. That is possible, although it is up to others to estimate those kinds of numbers. But the actual core process that exists now would continue to operate in that environment.[22]

22 *Committee Hansard*, 13 August 2003, p. 8.

Chapter Six

Fund Costs

Introduction

6.1 This chapter examines the impact of the portability regulations on fund costs, with specific reference to:

a) Multiple roll over/transfer costs;

b) Partial roll over/transfer costs; and

c) Revised benefit designs.

Multiple roll over/transfer costs

6.2 As indicated in Chapter One, regulation 6.33 of the draft Superannuation Industry (Supervision) Amendment Regulations 2003 allowed unlimited roll overs/transfers out of a superannuation account.

6.3 A large number of parties making submissions to the inquiry opposed this provision on the basis of its cost impact on funds. For example, the Law Council of Australia argued that the draft regulations would create an unnecessary administrative burden, and could result in members treating a superannuation interest like a bank account.[1]

6.4 In turn, ASFA argued that the introduction of portability without choice would create a new class of exiting member (a partial active-account exit), which would require funds to establish new processing arrangements with associated additional costs. ASFA noted that rather than just closing an account, funds would be required to make the roll over/transfer, update the member record to reflect the individual benefit component rolled over/transferred, record this as a regulation 6.33 request and so on.[2]

6.5 Similar concerns regarding higher fund costs were also raised by Mercer,[3] the AIG[4] and the Corporate Super Association.[5]

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1 *Submission* 20, Law Council of Australia, p. 3.

2 *Submission* 2, ASFA, p. 4.

3 *Submission* 17, Mercer, p. 3.

4 *Submission* 5, AIG, p. 2.

6.6 Given such concerns about the costs of portability, many parties to the inquiry further argued for limits to be placed on the number of roll overs/transfers available to fund members:

- IAA recommended that the Government assist funds to control costs by allowing trustees to limit the numbers of roll over/transfer requests from any member to no more than say, one a year.[6]
- MTAA Super advocated that any portability arrangements should require a minimum period (say 12 months) before a second and subsequent full or partial roll over/transfer of an account balance could be requested.[7]
- CPA Australia advocated that consideration be given to limiting the timing of when portability can be exercised, such as on resignation from an employer or no more than once a year.
- The FPA recommended that a member have a limit of, say, two roll overs/transfers per year, to overcome some of the cost burden on funds.[8]

6.7 As indicated in Chapter One, the Government moved in the gazetted regulations to require trustees only to affect one roll over/transfer per year for each member of a fund, although they will be free to offer more regular roll overs/transfers if they wish. The Committee notes that in the hearing on 1 August 2003, Mr Ward from Mercer[9] and Mr Shallue from IAA[10] welcomed the restriction on roll overs/transfers to one a year.

6.8 Nevertheless, some concerns about the impact of the portability regulations on fund costs remained. For example, Mr Silk from IFF observed in the hearing on 1 August 2003:

> In relation to the first issue—that is, a limit on the number of transfers to one per year—we submit that that is a significant improvement on the proposals contained in the original regulations. However, that is an improvement from a very low base. The original proposal—and we need not now go into the details—was fundamentally flawed and would have caused significant long-term damage to the retirement incomes of a number of Australians. It would have imposed significant additional cost pressures on the system as a whole that would have ultimately been borne by the members of superannuation funds.[11]

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5 *Submission* 9, Corporate Super Association, p. 5.

6 *Submission* 15, IAA, p. 3.

7 *Submission* 6, MTAA Super, p. 3.

8 *Submission* 24, FPA, p. 1.

9 *Committee Hansard*, 1 August 2003, p. 27.

10 *Committee Hansard*, 1 August 2003, p. 40.

11 *Committee Hansard*, 1 August 2003, p. 3.

6.9 Ms Galbraith from Superpartners also indicated that the restriction to one roll over/transfer in a year was a welcome change. However, she raised the following concern:

> If we have the scenario of members who are receiving ongoing contributions taking their entire account balance every 12 months, we will have to close that member's account and then when the next contribution comes in create a new account for them in the same fund. This causes a number of administration issues for us, the most pertinent being that it is difficult to carry the member's history across.[12]

6.10 In response to such arguments for restrictions on transfers, however, Mercer submitted that there is an argument for placing no restriction on the number of roll overs/transfers if portability is to work effectively for members, assuming the members paying an appropriate exit fee each time.[13]

6.11 APRA also acknowledged that members may seek regular roll overs/transfers out of a fund and that this would raise administration costs. Accordingly, APRA noted that trustees will need to ensure that administration systems (including those of service providers) are such that information (including on current member benefits and exit fees) can be given on request to prospective transferors, that inward and outward transfers can be effected and that disclosure requirements (including in relation to possible changes to insurance cover) are met.[14]

Partial roll over/transfer costs

6.12 Similar to concerns raised above about the impact of frequent fund roll overs/transfers on fund costs, a number of parties to the inquiry also highlighted the impact of partial roll overs/transfers on fund costs.

6.13 For example, Watson Wyatt argued that allowing partial roll overs/transfers of withdrawal benefits at any time will increase fund costs through additional benefit processing, investment costs and surcharge reporting. Accordingly, Watson Wyatt argued that the draft regulations should make it clear that the additional costs incurred from portability are able to be allocated equitably between those members who request a fund roll over/transfer.[15]

6.14 Similar concerns were expressed in hearings. For example, Mr Watson from MTAA Super indicated in the hearing on 31 July 2003:

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12 *Committee Hansard*, 1 August 2003, p. 13.

13 *Submission* 17, Mercer, p. 3.

14 *Submission* 14, APRA, p. 4.

15 *Submission* 12, Watson Wyatt, p. 2.

> Our view is that partial rollovers will actually create the opposite effect to what the regulations are seeking to do in terms of reducing the costs, increasing competition and improving the lot of members.[16]

6.15 Similarly, Dr Anderson from ASFA indicated in the hearing on 31 July 2003 her opposition to partial roll overs/transfers.[17]

6.16 Given these concerns, the Committee notes that a number of parties to the inquiry also recommended that partial roll overs/transfers be restricted or prohibited:

- AIST recommended that members be restricted to one partial roll over/transfer per year.[18]
- The Law Council of Australia suggested that the draft regulations ought to either prescribe the number of times annually a member can make a request for a partial roll over/transfer or give the trustee the power to determine how frequently a request can be made.[19]
- IAA recommended that trustees be given discretion to refuse requests for partial roll overs/transfers.[20]
- The CPA Australia advocated that individuals only be allowed to roll over/transfer the whole of their superannuation benefits, in the interests of maintaining a simple system and ensuring that the administrative burden on superannuation providers is minimised.[21]

6.17 Similar positions were also expressed in hearings. Ms Ryan from AIST indicated in the hearing on 31 July that short of the regulations being deferred to coincide with the introduction of choice, AIST would like roll overs/transfers, including partial roll overs/transfers, to be restricted to one a year.[22] Mr Shallue from IAA argued that trustees should be given further discretion to refuse requests for partial roll overs/transfers.[23]

6.18 Once again, the Committee notes that Government partially addressed this matter in the gazetted regulations by limiting the number of roll overs/transfers, including partial roll overs/ transfers, to one a year.

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16 *Committee Hansard*, 31 July 2003, p. 12.

17 *Committee Hansard*, 31 July 2003, p. 17.

18 *Submission* 11, AIST, pp. 2-3.

19 *Submission* 20, Law Council of Australia, p. 3.

20 *Submission* 15, IAA, p. 3.

21 *Submission* 13, CPA, p. 2.

22 *Committee Hansard*, 31 July 2003, p. 25.

23 *Committee Hansard*, 1 August 2003, p. 40.

Revised benefit design

6.19 In its written submission, Mercer argued that there are many funds which will need to change their benefit design in order to properly cater for portability. This will require advice to members and changes to trust deeds, product disclosure statements, other communication material, administration systems and so on. Mercer cited two examples:

a) One example is an accumulation fund where the death benefit is the greater of 5 times salary and the member's account balance. If the member elects to roll over/transfer part or all of the account balance, this would result in a higher level of insurance being required to maintain the pre-roll over/transfer benefit. It may therefore be appropriate (or necessary) for the benefit of 5 times salary to be similarly reduced. (If not reduced, then the higher level of insurance would have to be funded by the member, the employer or other members.)

b) A second example is a partially vested accumulation fund. In such a fund it would not be possible to merely reduce the partially vested account by the amount rolled over/transferred. Significantly more complex procedures would be involved.

6.20 Mercer submitted that changes in benefit designs will result in additional costs to funds from changing the governing rules, changing the administration systems, changing communication material and a more complex benefit design. Accordingly, Mercer argued that funds will need to be given at least 12 months to put appropriate systems in place.[24]

24 *Submission* 17, Mercer, p. 4.

Chapter Seven

Exit Fees

Introduction

7.1 This chapter examines three issues in relation to exit fees levied on superannuation funds in Australia:

a) Whether exit fees are a barrier to portability;

b) Whether a cap or ban should be placed on exit fees; and

c) The Government's position on exit fees.

A barrier to portability?

7.2 The application of exit fees, their level, and whether they pose a barrier to portability, attracted considerable comment and debate during the conduct of the inquiry.

7.3 For example, in its written submission, the ACA argued that exit fees are a true barrier to portability, and that their presence in the superannuation sector undermines any attempts to introduce greater mobility among consumers.[1]

7.4 Similarly, in its written submission, IFF argued that exit fees can act as a major obstacle to members seeking to roll over/transfer their superannuation, and cited the examples in Table 7.1 below of the cost of rolling over/transferring an amount from a non-industry fund to an active industry fund account.

Table 7.1: Exit Fees/Penalties cited by IFF

Account Balance	Exit Fee/Penalty	Per cent
$5,939.14	$5,621.11	95
$1,287.80	$1,195.27	93
$11,223.08	$8,211.53	73
$21,694.00	$6,090.67	28
$216,705.36	$40,595.40	19

Source: Submission 4, IFF, p. 2.

1 *Submission* 32, ACA, p. 3.

7.5 In its written submission, IFF argued that many people refuse to incur costs such as those listed in Table 7.1 above, and thus retain their money in their existing accounts.[2]

7.6 In its written submission, Cbus also indicated that it has identified withdrawal fees of up to $5,940 or 32 per cent of the balance of a fund for one of its members who wished to consolidate his or her account with Cbus.[3] Accordingly, Cbus also argued that the existence of significant exit fees acts as a barrier to competition.[4]

7.7 In response to such concerns, the Committee notes that IFSA made a detailed submission. IFSA argued that exit fees essentially fall into four broad categories:

a) Recovery of administration costs. IFSA indicated that completing a roll over/transfer requires significant administration to ensure that the roll over/transfer has been successful, that the receiving fund is a complying fund, that it will accept the roll over/transfer and so on. The fee is usually a fixed dollar fee.

b) Deferred entry fees. IFSA indicated that in some products, the investor may choose not to pay an entry fee, and instead to pay higher ongoing fees. The product provider pays the advice fee to the adviser up-front, and a reducing exit fee applies to recover the balance of the commission should the investor leave the fund within a set period, for example five years.

c) Early termination fees in closed products. IFSA indicated that these fees were used in superannuation products offered through life insurance offices to recover up-front costs by the life office. They were often calculated on the first year's premium and reduced over a set period of, say, five years.

d) Early termination of contract fees. IFSA indicated that traditional policies such as those offered during the 1980s were structured on a long-term basis, and included significant early termination fees or adjustments for early termination of contract.[5]

7.8 In relation to each of these categories of exit fees, IFSA argued that they no longer constitute barriers to members seeking to roll over/transfer their superannuation:

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2 *Submission* 4, IFF, p. 3.

3 *Submission* 16, Cbus, p. 3.

4 *Submission* 16, Cbus, p. 3.

5 *Submission* 21, IFF, pp. 3-4.

a) Recovery of administration costs: IFSA argued that these fees, which simply meet administrative and transaction costs, do not represent a barrier to exit. Indeed, it would be inequitable to subsidise such fees by charging the remaining members of the fund.

b) Deferred entry fees: IFSA argued that as deferred entry fees are generally flexible (investors can choose the structure they prefer) and reduce to zero over a period of up to five years, they do not represent a significant barrier to portability.

c) Early termination fee products: IFSA argued that products enforcing early termination fees were commonly offered during the 1980s, but that the life insurance industry has moved away from offering such products. IFSA argued that they constitute less than 5 per cent of all retail and master trust funds under management.

7.9 Accordingly, IFSA argued that exit fees do not represent a significant barrier to portability of superannuation accounts, and that a compelling case has not been made to regulate exit fees.[6]

7.10 Mr Gilbert from IFSA reiterated these arguments in the hearing on 31 July 2003, and further argued that the introduction of a competitive portability and choice environment would prevent products with high exit fees ever being offered in the future. In the past, Mr Gilbert suggested that many people offered products with high exit fees never had a choice about where the money went – it was directed to a particular fund by their employer.[7]

7.11 The above evidence of IFSA was reiterated by the ABA[8] and the FPA. The FPA additionally suggested that 'high' exit fees often reflect acquisition costs which have already been met and are recovered over the life of a contract. In addition, the FPA also submitted that making retrospective changes to existing contracts/agreements would have a major negative financial impact on the providing fund or sponsor.[9]

7.12 The Committee also notes that in the hearing on 1 August 2003, Mr Ward from Mercer indicated that in the hundreds of funds that Mercer administers, he is not aware of any that charge excessive exit fees. He noted that in some cases, the cost of realising the assets (sometimes up to 20 per cent) might be passed on to the member, and that that cost might be interpreted as an exit fee, however in practice it is not.[10]

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6 *Submission* 21, IFSA, pp. 3-4.

7 *Committee Hansard*, 31 July 2003, p. 29.

8 *Submission* 29, ABA, p 3.

9 *Submission* 24, FPA, p. 2.

10 *Committee Hansard*, 1 August 2003, pp. 26, 31.

7.13 In the hearing on 1 August 2003, the Committee raised with Mr Silk from IFF the argument of IFSA that the incidence of 'old-style' life company type superannuation products was declining. Mr Silk responded as follows:

> I understood that was put to the committee yesterday. In fact, I contacted Industry Funds Financial Practice this morning before this hearing to put that to them. They said that is certainly not the case. Certainly endowment policies are reducing as a proportion of policies in the community, but many of the instances that I have spoken of—and I have got pages of other examples here with similar amounts of money and similar percentage fees—are from modern day master trusts by many very well-known providers of master trust products. So, first, it is not a small problem. Second, it is not confined to endowment type policies. Third, it is a feature of large master trust products that are promoted by many of the industry's biggest players.[11]

Tabled document on exit fees

7.14 The Committee notes that further to the arguments about the level of exit fees outlined above, Mr Silk from IFF tabled in the hearing on 1 August 2003 a large number of further examples of exit fees/penalties (including those listed in Table 7.1 above). The tabled document is reproduced in **Appendix Seven**. Mr Silk obtained the figures from Industry Funds Financial Practice, which is an organisation which provides financial planning advice to members of industry superannuation funds.[12]

7.15 As shown in **Appendix Seven**, Industry Funds Financial Practice listed a large number of retail superannuation funds which it claimed levied exit fees of up to 95 per cent.

7.16 The Committee subsequently received a supplementary submission from IFSA responding to the document tabled by Mr Silk, and the claim of exit fees of up to 95 per cent. Based on consultation with the companies involved, IFSA argued that the document tabled by Mr Silk contained two significant errors.

7.17 Firstly, the tabled document claimed exit fees were levied by at least one fund that does not charge any exit fee, and which had never charged any exit fee.

7.18 Secondly, the funds referred to were not modern day master trusts as asserted by Mr Silk. IFSA commented as follows:

> IFSA can find no example in the tabled list of an exit fee levied in master trusts open to new members, as the witness appears to have asserted. Critically, the implication that investors who join master trusts now could be levied exit fees of the levels listed in the document is false. There are closed, old-style products where the member has 'traded up' to a master trust environment while retaining the existing contract conditions. IFSA is

11 *Committee Hansard*, 1 August 2003, p. 5.

12 *Committee Hansard*, 1 August 2003, p. 4.

> advised that no new member of a master trust, even where the master trust now encompasses these traded-up policies, can face an exit fee such as those claimed in the tabled document.[13]

7.19 Based on these two arguments, and possibly confusion of exit fees for tax by the Industry Funds Financial Practice, IFSA argued that the Committee should draw no conclusions from the document tabled by Mr Silk.[14]

7.20 For completeness of the record, the Committee publishes the supplementary submission of IFSA in response to the document tabled by Mr Silk in **Appendix Eight**.

7.21 In turn, the Committee also received a supplementary written submission from IFF in which it stood by its tabled document.[15] The IFF's supplementary submission was prepared for IFF by Industry Funds Financial Planning (IFFP), and analysed the recommendations made by the IFFP Rollover Service concerning exit penalties charged by other funds for the period 1 July 2001 to 30 June 2003.

7.22 The IFFP found that from 1 July 2001 to 30 June 2003, the Rollover Service produced a total of 2310 recommendations:

- Of the 2310 recommendations, 387 (16.8 per cent) were recommendations not to roll over. Of those 387 recommendations:
  - 194 were due to exit penalties. The total value of exit penalties was $747,994, or 19 per cent of the corresponding account balances of $3.9 million.
  - 193 were due to issues other than exit penalties.
- Of the 2310 recommendations, 1923 (83.2 per cent) were recommendation to roll over, of which 1196 involved no exit penalty and 727 (37.8 per cent of all roll over overs) involved an exit penalty.
  - Of the 727 recommendations to roll over despite an exit penalty, the total value of exit penalties was $626,982 or 34.5 per cent of the value of the corresponding total account balance ($18.2 million).

7.23 Again, for completeness of the record, the Committee published the supplementary submission of IFF in **Appendix Nine**.

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13 *Submission* 30, IFSA, pp. 1-2.

14 *Submission* 30, IFSA, p. 2.

15 The original submission was received 14 August 2003. The Committee subsequently received additional supplementary material by post on the 18 August 2003.

A cap or ban on exit fees?

7.24 A large number of parties to the inquiry advocated that a cap be placed on exit fees on mandated superannuation products at a level sufficient to cover actual expenses to a fund from a roll over/transfer. To cite the ACA submission:

> In ACA's view, if the industry cannot evolve to abolish these fees, there is a strong case for Government intervention. Australian consumers do not have a choice about contributing to superannuation – it is mandated by government, and if they are to be given the power to exercise greater control over the location of their superannuation, they should not be fined for doing so.[16]

7.25 This position was expressed by SOS,[17] AIG,[18] the Corporate Super Association,[19] the ACTU,[20] AIST[21] and IFF.[22]

7.26 Importantly, however, the Committee notes that in its written submission, Mercer specifically rejected an outright ban on exit fees. Mercer argued that the additional costs associated with portability will generally be recouped by charging an exit fee to members who elect to roll over/transfer benefits. If an exit fee is not charged, Mercer noted that this would lead to other members subsidising the costs of the transferring members, which would be inequitable. [23]

7.27 This position was reiterated by Mr Smith from the Queensland Local Government Superannuation in the hearing on 31 July 2003:

> … the people that want to have the portability should be bearing that additional cost in some shape or form and that as much as possible the people that stay with the fund long term should not bear a disproportionate share of that cost.[24]

7.28 The Committee also noted evidence from the hearings that any cap on exit fees to, say, the cost of processing, would have to be prospective rather than retrospective.[25]

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16 *Submission* 32, ACA, p. 3.

17 *Submission* 19, SOS, p. 1.

18 *Submission* 5, AIG, p. 1.

19 *Submission* 9, Corporate Super Association, p. 5.

20 *Submission* 10, ACTU, p. 1.

21 *Submission* 11, AIST, p. 2.

22 *Submission* 4, IFF, p. 3.

23 *Submission* 17, Mercer, p. 3.

24 *Committee Hansard*, 31 July 2003, p. 48.

25 *Committee Hansard*, 31 July 2003, p. 23. *Committee Hansard*, 1 August 2003, p. 6.

7.29 In the hearing of 1 August 2003, Mr Ward from Mercer, which administers hundreds of funds, suggested that the real cost of providing a roll over/transfer is probably greater than $100 but less than $200.

7.30 In response to these arguments, IFSA suggested that regulation of exit fees would be counter productive from a competition, choice and consumer design perspective. If a cap was placed on fees, IFSA argued that fees would tend to rise to match the level of the cap.[26]

The Government's position

7.31 The Committee raised the issue of exit fees with officers of Treasury in the hearing on 13 August 2003.

7.32 In his evidence, Mr Rosser from Treasury acknowledged that in some circumstances, depending on the level of the fee, exit fees can constitute a barrier to portability. However, Mr Murray argued that the Government cannot retrospectively address exit fees in a contract that individuals have entered into.[27] In addition, Mr Murray argued that if exit fees were banned, it may well be that the exit fee cost would simply be translated into an additional annual administration cost which all members of the fund would bear, instead of the member exiting the fund.

7.33 Rather, Mr Murray expressed the Government's position on exit fees as follows:

> …the government's view is that the actual competition that will flow from portability will ensure that funds in future will not be charging high exit fees. They will not attract new members if they do.[28]

7.34 In its written submission, APRA also suggested that the introduction of portability may foster competition in the industry by forcing funds to be more sensitive towards fee structures and investment performance.[29]

7.35 In response to the stated Government position on exit fees, Senator Sherry argued that if fund trustees wanted to keep members and their superannuation savings within the fund, then the logical thing for the trustees to do would be to introduce a high exit fee. This would be especially attractive to some fund trustees who are presently guaranteed a certain employer contribution, such as funds under state awards.[30]

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26 *Submission* 21, IFSA, pp. 3-4.

27 *Committee Hansard*, 13 August 2003, p. 26.

28 *Committee Hansard*, 13 August 2003, p. 25.

29 *Submission* 14, APRA, p. 3.

30 *Committee Hansard*, 13 August 2003, pp. 26-28.

7.36 In reply, Mr Murray and Mr Rosser from Treasury acknowledged that there would be no legislative restriction on trustees placing high exit fees to prevent roll overs/transfers, but that they would have difficulty attracting new members. Mr Rosser suggested that fund trustees would be unlikely to effectively close their fund through a high exit fee in a competitive environment.[31]

7.37 The Committee notes that in its September 2002 consultation paper, Treasury indicated that the Government's preference is to allow funds to develop their own fee structures, but that the Government would reserve the right to regulate exit fees if this appeared necessary to ensure the effectiveness of portability.[32]

31 *Committee Hansard*, 13 August 2003, pp. 26-27.

32 Commonwealth Treasury, *Portability of Superannuation Benefits*, p. 16. *Committee Hansard*, 13 August 2003, p. 28.

Chapter Eight

Fund Investments and Returns

Introduction

8.1 This chapter examines three issues in relation to the likely impact of the portability regulations on fund investments and returns:

a) Fund investments and liquidity;

b) Smoothed investment returns; and

c) Capital guarantees.

Fund investments and liquidity

8.2 In its written submission, MTAA Super expressed concern that if the draft portability regulations were introduced, funds would be judged only on their latest credit rates – even their last monthly interim return. In turn, MTAA Super argued that this could lead to trustees having to seek out shorter term investments, to the detriment of long-term retirement incomes and Australia's retirement income investment pool generally.[1] This matter was also raised by Mr Watson from MTAA Super in the public hearing on 31 July 2003.[2]

8.3 MTAA Super also argued in its written submission that higher levels of churning between funds would require funds to retain more liquid assets so as to be able to meet their liquidity obligations under the SIS Act. In turn, highly liquid assets such as cash and fixed interest generally under perform growth assets such as shares, property and infrastructure over the mid to long term. As a result, forcing funds to maintain more liquid assets would lead to lower long-term average returns.[3] Once again, this matter was raised by Mr Watson from MTAA Super in the hearing on 31 July 2003.[4]

8.4 Similar concerns were expressed by the Corporate Super Association in its written submission. The Association noted that trustees, when formulating their

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1 *Submission* 6, MTAA Super, p. 4.

2 *Committee Hansard*, 31 July 2003, p. 7.

3 *Submission* 6, MTAA Super, p. 4.

4 *Committee Hansard*, 31 July 2003, p. 10.

investment strategies, are required under section 52 of the SIS Act to take into account:

- Expected cash flow liabilities; and
- The ability to discharge liabilities when they fall due.

8.5 The Association suggested that currently, most employer sponsored funds would base their investment strategies on the assumption that members will remain with the fund while their employment with their sponsor lasts. Accordingly, trustees seek to maximise returns according to the age and average service length of the fund's membership, which determine anticipated liquidity requirements.

8.6 However, the Association argued that ready portability of benefits would alter the liquidity requirements of a fund. In general terms, the anticipated period of membership would be expected to decline and the timing of exits from the fund would be less predictable. As a result, trustees would be required to keep more funds in liquid assets, with an associated reduction in fund returns.[5]

8.7 These issues were also raised by other parties, including AIG[6] and AIST.[7] In addition, the Committee notes the evidence of Ms Ryan from AIST in the hearing on 31 July 2003:

> A lot of the infrastructure investments—which are proving to be good investments, although it takes quite a few years for the returns to come in—would be undermined if a fund had to keep 25 per cent or more of its accumulated funds liquid so that that money could be rolled out as members chose to roll their money out.[8]

8.8 In response to this issue of fund investment and liquidity, the Committee notes the evidence of Mr Gilbert from IFSA in the hearing on 31 July 2003:

> Clearly, infrastructure assets are listed on the Australian Stock Exchange, have a daily price and can be redeemed overnight. So I do not see that there is any danger to infrastructure investments as a consequence of portability. I think that borders on being a red herring.[9]

8.9 On a related issue, in its written submission, CPA Australia argued that the portability regulations should offer funds some protection from members who opt for long-term strategies for their superannuation investments, but then wish to withdraw their superannuation benefits on a short-term basis.

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5 *Submission* 9, Corporate Super Association, p. 6.

6 *Submission* 5, AIG, p. 2.

7 *Submission* 11, AIST, p. 3.

8 *Committee Hansard*, 31 July 2003, p. 20.

9 *Committee Hansard*, 31 July 2003, p. 33.

8.10 In response, however, Cbus indicated in its written submission that it is satisfied that the liquidity risk to a superannuation fund resulting from the introduction of the draft regulations has been addressed by allowing a fund to apply to APRA to suspend roll overs/transfers where they could impact on the financial position of the fund.[10] The Committee notes that these provisions remain substantially unchanged in the gazetted regulations.

Impact on Trustees

8.11 In its written submission, APRA acknowledged that to facilitate roll overs/transfers under the portability regulations, trustees of funds may be forced to realise assets which are not liquid in a less than favourable market. APRA stated that this will entail a lower rate of return on the realised asset, and therefore disadvantage the interests of remaining members. Accordingly, APRA noted in relation to the draft regulations that:

- Trustees will need to review fund liquidity to support portability requests. This will involve review of investments and investment strategies to ensure that adequate levels of liquid assets are available and consistent with potentially increased numbers of outward roll overs/transfers.
- The situation may arise where trustees, in adjusting investment strategies to take into account portability, may attempt to offset the need for increased liquidity by taking on extra risk in other areas of the portfolio in an endeavour to increase investment returns. Trustees must ensure that these adjustments are consistent with the objectives of the fund.[11]

8.12 This matter was reiterated by Mr Brunner from APRA in the public hearing on 13 August 2003.[12]

Smoothed investment returns

8.13 In its written submission, the Corporate Super Association raised the issue of smoothed investment returns. Smoothing investment returns refers to the practice of some funds using investment reserves to reduce fluctuations in crediting rates on accumulation balances from year to year. The objectives are to promote fairness between members and/or to promote the understanding that returns are stable over time.

8.14 However, the Corporate Super Association suggested that under a portability regime, fund members could time their departure from a fund at the point where reserves have been allocated, and re-enter when reserves have climbed again. This

10 *Submission* 16, Cbus, p. 5.

11 *Submission* 14, APRA, p. 4.

12 *Committee Hansard*, 13 August 2003, p. 33.

would reduce equity between members, forcing funds to abandon the smoothing of investment returns, with its associated benefits.

8.15 Accordingly, the Association recommended that portability should not apply to accumulation balances which are subject to a smoothing of investment returns, whether or not the balances are linked to a defined benefit fund.[13]

8.16 This issue was also raised by AAS in its written submission. AAS reiterated that funds that used smoothing of investment returns may have to alter their investment strategy to hold higher levels of cash, to the detriment of ongoing members. This is because members' long term retirement savings will need to be effectively 'at call' in a portability environment.[14]

8.17 The Committee notes that the Queensland Local Government Superannuation Scheme is a good example of a superannuation scheme providing smoothed investment return. Over the year to 30 June 2003, the scheme's growth fund made a return of -1.7 per cent. However, with the growth smoothing strategy calling on reserves, the fund is crediting 2.04 per cent over the year to 30 June 2003. However, Mr Smith from the Queensland Local Government Superannuation Board argued that under the portability regulations:

> If people can move out [of the fund], we would have to forego smoothing and it would be very difficult because people would be selecting against us going in and out and so on.[15]

Capital guarantees

8.18 In its written submission, the Corporate Super Association raised the issue of capital guarantees applying to an accumulation interest in a defined benefit fund. The Association suggested that it is open to a member to use the protection of a capital guarantee for a period when returns are uncertain, and then to move to another fund when market conditions improve.

8.19 The Association further indicated that it is aware of at least one instance of a fund which offers a capital guarantee as described above which under the draft portability regulations would need to approach APRA to have the fund's ability to roll over/transfer amounts suspended under draft regulation 6.37. Failing that, the Association suggested that the fund would have to remove its capital guarantee in order to ensure equity between members.

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13 *Submission* 9, Corporate Super Association, p. 7.

14 *Submission* 18, AAS, p. 7.

15 *Committee Hansard*, 31 July 2003, p. 46.

8.20 Accordingly, the Association recommended that portability should not apply to accumulation balances which are subject to a capital guarantee, whether or not the balances are linked to a defined benefit fund.[16]

16 *Submission* 9, Corporate Super Association, p. 7.

Chapter Nine

Commission-based selling

Introduction

9.1 This chapter examines two issues:

a) Commission-based selling, and concerns that the portability regulations could lead to increased churning of accounts to the benefit of financial planners; and

b) The impact of the portability regulation on not-for-profit funds.

Commission-based selling

9.2 It its September 2002 consultation paper, Treasury noted that 'Portability would increase the importance of financial advisers in the selling of superannuation'. A number or parties raised issues relating to financial advisers and commission-based selling during the inquiry.

9.3 In its written submission, AAS argued that many financial planners are reluctant to recommend non-profit superannuation funds, such as industry funds, which do not pay commissions. In support of this argument, AAS cited the findings of the recent ASIC/ACA Survey on the Quality of Financial Advice Planning. AAS cited the following passages from the report:

> A common observation by several judges was that clients' interests did not appear to be the sole factor in the plan strategy or product selection. … Recommendations frequently overlooked options that may be more cost-effective … low cost superannuation funds – never recommended; …
>
> Many plans did not recommend the lowest cost option available. As low cost options pay no commission, this raised some suspicions about the influence of commission on advice. For example, no adviser recommended switching to a non-profit, industry superannuation fund.[1]

9.4 Similarly, the ACA[2] and the Corporate Superannuation Association also referred to the ASIC/ACA Survey on the Quality of Financial Advice Planning. The Corporate Superannuation Association commented:

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1 *Submission* 18, AAS, p. 6.

2 *Submission* 32, ACA, p. 4.

> The ACA's findings suggested that a significant number of planners involved in the survey did not take sufficient account of their clients' needs and objectives and made investment recommendations without apparent justification (seemingly to earn the planner commissions).[3]

9.5 The Committee also notes the evidence of Ms Galbraith from Superpartners in regard to the ASIC/ACA report. Ms Galbraith indicated that 48 per cent of people surveyed who preferred commission-based advice as opposed to up-front fees thought it would motivate the adviser to give better advice. They did not appreciate that the commission was based on the initial placement and ongoing capital inflows, regardless of how well or badly the investment performed.[4]

9.6 Given these concerns in relation to commission-based selling, the Corporate Superannuation Association argued that the introduction of the portability regulations could increase the likelihood of fund members being persuaded by financial advisers to move their savings around either once or repeatedly, the principal advantage of which would accrue to the advisers in the form of commissions (to the detriment of individuals).[5] This was reiterated by Mr Brookes from the Corporate Superannuation Association in the hearing on 1 August 2003:

> Our real concern with portability and choice of fund is that the mechanisms at the moment are corrupt. They are corrupted by self-interest, generally, in the advice being given, which is profit driven.[6]

9.7 Similarly, Dr Anderson from ASFA stated in the hearing on 31 July 2003:

> In a portability regime, as in a choice regime, uninformed consumers would be vulnerable to unscrupulous people interested in their own wealth creation, not the client's.[7]

9.8 In response to this issue, the Committee notes that in their written submissions, AIST[8], IFF[9] and Cbus[10] all recommended a ban on commission-based roll overs/transfers of <u>mandated</u> employer superannuation contributions. The MTAA Super advocated a ban on commission-based selling of superannuation products where

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3 *Submission* 9, Corporate Super Association, p. 4.

4 *Committee Hansard*, 1 August 2003, p. 16.

5 *Submission* 9, Corporate Super Association, p. 4.

6 *Committee Hansard*, 1 August 2003, p. 36.

7 *Committee Hansard*, 31 July 2003, p. 14.

8 *Submission* 11, AIST, p. 2.

9 *Submission* 4, IFF, p. 4.

10 *Submission* 16, Cbus, pp. 2,3.

the taking of that product would lead to higher management fees or charges than in the member's current fund. In effect, this would be a 'no detriment test'.[11]

9.9 Support for a ban on commission-based roll overs/transfers of mandated employer superannuation contributions was reiterated in hearings by Mr Watson from MTAA Super,[12] Mr Silk from IFF and Ms Hewett from Cbus. Ms Hewett stated in the hearing on 1 August 2003:

> We understand that there are about 15,000 financial advisers in Australia and most of those are remunerated with some configuration that includes a commission base. … We think that financial planners can play a very constructive and very positive role if there is no conflict of interest, but our experience, again, has shown that very often there is a conflict of interest between getting a good retirement outcome for the member and making sure that the financial planner's remuneration is maintained. We see this as a problem in a commission based environment, and we think that commissions should not apply to mandatory contributions.[13]

9.10 Similarly, Mr Silk from IFF stated in the hearing on 1 August 2003:

> But, more fundamentally, we submit, as I have indicated in our written submission and also have said today, that there should not be commissions—which is the major issue at play in terms of contracts—on mandated employer contributions. If the federal parliament dictates that employers should pay nine per cent of an employee's wage or salary into a superannuation account then we say it is entirely inappropriate for third parties to excessively enrich themselves at the expense of the intended beneficiary of those payments.[14]

9.11 Although not advocating a ban on commission-based selling, in its written submission, Taxpayers Australia advocated that the regulators will need to be vigilant regarding possible churning of accounts and inappropriate recommendations from financial advisers.[15]

9.12 In response to some of these concerns, Mr Hristodoulidis noted that Section 947D of the new FSR Act makes it clear that the Government will not tolerate churning of fund members by financial advisers. Mr Hristodoulidis also cited the recently released ASIC policy statement No. 175, entitled 'Licensing: financial product advisers—conduct and disclosure', paragraph 175.91 of which states:

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11 *Submission* 6, MTAA Super, p. 6.

12 *Committee Hansard*, 31 July 2003, pp. 6-7.

13 *Committee Hansard*, 1 August 2003, p. 20.

14 *Committee Hansard*, 1 August 2003, p. 6.

15 *Submission* 23, Taxpayers Australia, p. 2.

> In the case of advice to replace one product with another product or to switch between investment options within a product, [ASIC] consider that the advice will generally be inappropriate if the providing entity knew or ought reasonably to have known that the overall benefits likely to result from the new product or option would be lower than under the old product or option. This applies where either or both the new product or the old product is a financial product for the purposes of part 7.7. Of course, [ASIC] would be unlikely to reach this view where there are overall cost savings to the client that are likely to override the loss of benefits. The determination of whether there are overall cost savings for the client must take into account all the circumstances, including the costs of the replacement i.e. making the switch.[16]

9.13 The FPA also indicated in its written submission that it has recently launched a national strategy called the Professional Partner Program aimed at 'raising the bar' in relation to professional standards in the financial planning community. The program will include five campaigns which will target disclosure, professionalism, advice, the FSR Act transition and consumer issues.

9.14 In launching the first campaign on disclosure, the FPA has established an industry taskforce to review disclosure issues in the Australian financial planning industry, including remuneration and benefits. The taskforce will make recommendations to the FPA Board of Directors on improvements to the principles and practices of disclosure of adviser remuneration and other benefits as well as factors likely to influence advisers in the provision of advice.[17]

9.15 The Committee notes that these matters were reiterated by Mr Hristodoulidis from the FPA in the hearing on 31 July 2003.

> …the success of the professional partner program relies on acceptance by all stakeholders. To this end, the program was developed in consultation with our members and other key stakeholders. We surveyed our members on the final program and found very strong support. Over 90 per cent of members either strongly or very strongly endorsed the program. Under the FPA's professional partner reform program, the FPA has today announced a major initiative in the drive for greater professionalism. We are committed to promoting the CFP designation as the mark of distinction of a professional financial planner and the highest membership designation bestowed on individuals who meet the high standards of education, examination, experience and ethics. The CFP is the highest internationally recognised designation for financial planners in Australia. There are already 5,000 CFPs practising in Australia, and it is expected that this number will

16 Cited in *Committee Hansard*, 31 July 2003, p. 61.

17 *Submission* 24, FPA, p. 4.

> continue to rise, with more than 800 students having enrolled in the CFP program each semester in the last 12 months.[18]

9.16 Finally, the Committee notes that in its written submission, APRA indicated that it would be concerned if implementation of the portability regulations led to commercially driven interests placing pressure on uninformed superannuation fund members to move their super where this would not be in their best interests. Accordingly, APRA supported the measures that the Government has previously outlined in relation to an education program as well as disclosure requirement under the FSR Act.[19]

Not-for-profit funds

9.17 Following on from the concerns raised above in relation to commission-based selling, the Corporate Super Association argued that the portability regulations would promote a one-way flow of funds out of not-for-profit employer-sponsored superannuation funds into retail funds.[20]

9.18 The basis of this concern expressed by the Corporate Super Association was that retail funds can promote themselves to the public and invite members. Not-for-profit funds, on the other hand, by their nature are established and operate under an arrangement between the trustee and the employer-sponsor and do not seek roll overs/transfers from the general public.

9.19 The Association further suggested that given the ongoing fees paid by members of retail funds and additional costs of moving funds, a one-way flow of funds out of not-for-profit employer-sponsored superannuation funds would result in lower overall retirement savings for Australians.[21]

9.20 This issue was reiterated by Mr Brookes from the Corporate Super Association in the hearing on 1 August 2003:

> The signs are there, and it is happening already, whereby the financial conglomerates occupy the key positions around which portability and choice of fund govern the field. To counter that, to have balance, we should have a position where the not-for-profit sector is not eliminated and is not obliged to be for-profit as the only way to survive. The not-for-profit sector itself can give generic advice, dispassionately and disinterestedly, to its members. That to us is the key issue. If we do not cross that bridge, it will be the end

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18 *Committee Hansard*, 31 July 2003, p. 61.

19 *Submission* 14, APRA, p. 5.

20 *Submission* 9, Corporate Super Association, p. 6.

21 *Submission* 9, Corporate Super Association, p. 6.

> of the not-for-profit provision of super and the end of the best deal for Australians.[22]

9.21 In its written submission, AAS also raised the issue of not-for-profit funds. AAS indicated that the majority of its clients are industry funds which charge fees at a level to recoup costs. As such, they have less resources for marketing compared to large, retail providers.

9.22 Accordingly, AAS argued that retail funds with large marketing budgets would be the greatest beneficiaries of the portability regulations, with non-profit funds potentially the largest losers.[23] Again, this was reiterated by Mr Korchinski from AAS in the hearing on 31 July:

> … we have concerns that members may be severely disadvantaged, because retail superannuation providers with large marketing budgets would be the greatest beneficiaries of a portability regime and the members of non-profit funds would potentially be the largest losers. Many financial planners are reluctant to recommend non-profit superannuation funds, such as industry funds, which do not pay commissions.[24]

9.23 Finally, the Committee also notes the evidence of Capt. Woods from SOS in the hearing on 31 July 2003. He argued that with the drive towards portability and choice, corporate funds are going to be faced in the not too distant future with the option of either competing in the market place or outsourcing their superannuation obligations. Prior to that happening, Capt. Woods argued that the representative industrial association should be given an opportunity to negotiate with the large corporate funds in order to allow those funds and their representative bodies to build new industry funds that provide economies of scale.[25]

22 *Committee Hansard*, 1 August 2003. p. 37.

23 *Submission* 18, AAS, pp. 5-6.

24 *Committee Hansard*, 31 July 2003, p. 52.

25 *Committee Hansard*, 31 July 2003, p. 67.

Chapter Ten

Application of the Regulations

Introduction

10.1 This chapter examines the application of the portability regulations with respect to:

a) Defined benefit schemes;

b) Unfunded public sector superannuation schemes;

c) Member benefit protection; and

d) The Queensland Local Government Superannuation Scheme.

Defined benefit schemes

10.2 Under regulation 6.30(2)(c) of the Superannuation Industry (Supervision) Amendment Regulations 2003, it is proposed that portability will not apply:

> In respect of a defined benefit component of a superannuation interest in a defined benefit fund, if the member who holds the interest is an employee of an employer-sponsor of the fund.

10.3 The Committee notes that regulation 6.30(2)(c) differs from the draft regulation released on 27 May 2003. The draft regulation stated that portability would not apply:

> In respect of a defined benefit component of a superannuation interest in a defined benefit fund, if the member who holds the interest is eligible to contribute to the fund under the governing rules of the fund.

10.4 In its supplementary written submission, Watson Wyatt welcomed the gazetted regulation as redressing the issues it raised in its initial written submission in relation to the draft regulation. Specifically, Watson Wyatt indicated that the gazetted regulation 6.30(2)(c):

a) Removes the considerable problems that would have been caused if defined benefit entitlements were subject to portability; and

b) Addresses the inconsistency between exempting contributory defined benefit arrangements and not exempting non-contributory defined benefit arrangements.[1]

10.5 The Committee notes that Mr Shallue from IAA also supported the exemption of defined benefit components under the gazetted regulations.[2]

10.6 However, in its supplementary written submission, Watson Wyatt expressed concern that the gazetted regulations raise a new issue. Watson Wyatt indicated that it is quite common for a defined benefit fund in Australia to have a benefit design that provides:

a) On resignation prior to the attainment of a specified period of service or age, a benefit that is accumulative in nature (eg. a benefit that is the sum of a member account and a company account, or a benefit that is expressed as a multiple of member account); or

b) On attainment of the specified period of service or age, a benefit that is defined benefit in nature (eg. a benefit based on a certain factor multiplied by years of service multiplied by average salary).

10.7 Watson Wyatt submitted in its supplementary submission that such interests should be classified as defined benefit components for the purposes of regulation 6.30(2)(c), even where the member's current entitlement is in accumulation form (as outlined in point 'a' above).[3] The Committee notes that this issue was also raised by Mr Shallue from IAA in the hearing on 1 August 2003:

> There was a minor change to the wording in the regulations yesterday, but on my reading I do not think it addresses the issue that we were trying to get to. … the difficulty is that a common defined benefit is designed to have a resignation benefit, which might be determined as an accumulation type benefit with a defined salary related benefit on retirement. So a defined benefit component may have a withdrawal benefit that is not defined by reference to salary or one of the other items referred to but it may have a retirement benefit component that is. In our view that would still be a defined benefit component.[4]

Unfunded public sector superannuation schemes

10.8 Regulation 6.30(2)(b) of the Superannuation Industry (Supervision) Amendment Regulations 2003 provides that the regulations do not apply to an

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1 *Submission* 27, Watson Wyatt, p. 1.

2 *Committee Hansard*, 1 August 2003, p. 39.

3 *Submission* 27, Watson Wyatt, p. 2.

4 *Committee Hansard*, 1 August 2003, p. 39.

unfunded public sector superannuation scheme. In turn, subregulation 1.03(1) inserts a definition of unfunded public sector superannuation schemes as:

> … a regulated superannuation fund that is declared to be an unfunded defined benefits superannuation scheme under regulation 2A of the *Superannuation Contributions Tax (Assessment and Collection) Regulations 1997*.

10.9 In its written submission, the Government Employees Superannuation Board of Western Australia noted that Part 1 of Schedule 1 of the *Superannuation Contributions Tax (Assessment and Collection) Regulations 1997* refers to two Acts in relation to Western Australia:

a) The *Government Employees Superannuation Act 1987*; and

b) The *Superannuation and Family Benefits Act 1938*.

10.10 However, the Board noted that both these Acts have been repealed and the schemes established under them continued under the WA *State Superannuation Act 2002*. This amendment is not reflected in the *Superannuation Contributions Tax (Assessment and Collection) Regulations 1997*.

10.11 Accordingly, the Board suggested that the *Superannuation Contributions Tax (Assessment and Collection) Regulations 1997* be amended to reflect current legislative circumstances.[5]

10.12 The Government Employees Superannuation Board of Western Australia also noted the proliferation of definitions in Commonwealth legislation relating to superannuation schemes administered by the states:

a) The superannuation schemes administered by Western Australia are prescribed as '*constitutionally protected funds*' in the *Income Tax Regulations 1936*, reflecting the limits placed on the Commonwealth's taxing powers by the Constitution.

b) Schemes established under Commonwealth, State or Territory Law are referred to as '*exempt public sector schemes*' in Schedule 1AA of the *Superannuation Industry (Supervision) Regulations 1994*, for the purposes of concessional taxation treatment under the *Income Tax Assessment Act 1936*.

c) As discussed above, the term '*unfunded public sector superannuation scheme*' is used in the *Superannuation Contributions Tax (Assessment and Collection) Regulations 1997* in relation to the assessment and collection of the superannuation surcharge.

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5 *Submission* 3, Government Employees Superannuation Board of Western Australia, p. 1.

10.13 Accordingly, the Board suggested that for the purposes of interpreting the application of Commonwealth legislation, and to avoid confusion, the Government should consolidate the terms used to refer to superannuation schemes administered under Commonwealth, State or Territory Law.[6]

Member benefit protection

10.14 Member benefit protection standards aim to prevent small superannuation benefits from being eroded by fees and charges. In general, the standards provide that if a member's withdrawal benefit is less than $1000, the fund must 'protect' it by limiting any fees and charges. In effect, this is a compulsory cross-subsidisation of members with small accounts by those with larger accounts.

10.15 However, regulation 1.03B(3) of the Superannuation Industry (Supervision) Amendment Regulations 2003 amends the definition of a 'protected member' as follows:

> If the trustee of a regulated superannuation fund has rolled over or transferred an amount that is the whole or part of a member's withdrawal benefit to another regulated superannuation fund or to an approved deposit fund, RSA or EPSSS in accordance with Division 6.5, the member is not a protected member of the fund from which the amount was rolled over or transferred.

10.16 As indicated earlier in this report, the gazetted regulations provide that if a member of a superannuation fund wishes to make a partial roll over/transfer (less than their entire withdrawal benefit), the trustee can require the member to leave a balance of up to $5,000 behind in the fund.

10.17 The Committee notes the evidence of Mr Korchinski from AAS on 31 July 2003 that the new $5,000 limit has obviated the concerns of AAS in relation to member benefit protection costs. AAS had originally been concerned that members would leave less than $1,000 in the fund, resulting in a higher member protection cost for the fund.[7] Similarly, Mr Silk from IFF observed in the hearing on 1 August 2003:

> Aside from family law considerations, the requirement for a $5,000 minimum account balance to be retained would serve to protect the member benefit protection interests of the fund from which the transfer was occurring albeit, depending on the amount of money transferred out of the fund, member benefit protection costs may still be incurred by the fund into which the money is to be transferred.[8]

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6 *Submission* 3, Government Employees Superannuation Board of Western Australia, p. 2.

7 *Committee Hansard*, 31 July 2003, p. 57.

8 *Committee Hansard*, 1 August 2003, p. 3.

The Queensland Local Government Superannuation Scheme

10.18 In its supplementary written submission, the Queensland Local Government Superannuation Board, which is trustee of Queensland Local Government Superannuation Scheme (LG Super), noted that under section 1183 of the *Local Government Act 1993* (Qld), all permanent employees of Queensland Local Government must be members of LG Super. They must contribute 6 per cent of their salary to the scheme, while participating employers currently contribute 12 per cent of the member's salary (3 per cent in excess of the SG requirement). LG super has about 21,000 members in an accumulation benefit fund, and about 9,000 members in a defined benefit fund.

10.19 Significantly, the Board indicated that as a scheme to which employers are required by state legislation to contribute at a rate in excess of the SG, the Board understood that LG Super was to be excluded from the operation of the Government's choice of fund legislation. However, under the draft regulations, LG Super's 21,000 members in the accumulation benefit fund would be covered by portability (the 9,000 members in the defined benefit fund are excluded).[9]

10.20 The Committee notes that this was reiterated by Mr Smith from the Queensland Local Government Superannuation Board during the hearing on 31 July 2003. Mr Smith advised that in 1998, the office of the Assistant Treasurer indicated in written advice to the Board that the special circumstances of the fund warranted a specific exclusion from the operation of the proposed choice of fund legislation.[10]

10.21 In turn, the Queensland Local Government Superannuation Board raised in its written submission the possibility that under the portability regulations, employers and unions may reconsider the payment of contributions in excess of SG if there is potential for those contributions to be moved to another fund, while presumably incurring costs for LG Super.

10.22 To emphasise this concern, the Queensland Local Government Superannuation Board further cited the findings of a review conducted in 2002 for the National Competition Policy into the potential anti-competitive provisions of the *Local Government Act 1993* (Qld):

> During the course of the review, stakeholders expressed strong support for retaining the current arrangements as a means to meet the objectives of the legislation and maximise benefits of the LGSS to its members. Furthermore, stakeholders participating in the consultation process (which included councils, the LGAQ, unions, the Board and Queensland Government Super Office) did not regard the LGA as restricting competition in a way that was detrimental to maximizing benefits to LGSS members.

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9 *Submission* 7, Queensland Local Government Superannuation Board, pp. 2-3.

10 *Committee Hansard*, 31 July 2003, p. 42.

> In sum, the review found that … maintaining the status quo has the broad support of stakeholders, has demonstrated net benefits to date and is regarded as the best option for achieving the public interest objective of section 1189(1). (This) option… also supports Queensland's Priority Outcome. The retention of section 1189 (1) is therefore recommended as a result of this review.[11]

10.23 In the hearing on 31 July 2003, Mr Carpendale from the Queensland Local Government Superannuation Board argued that unless LG Super's 21,000 members in the accumulation benefit fund were excluded from the operation of the portability regime, the fund would face the following issues:

a) Firstly, an inefficient and disruptive disconnection between what members can do with their accrued benefits under the portability regulations, and what they can do with their ongoing contributions under the proposed choice of fund regime.

b) Secondly, the economies of scale achieved by LG Super to the advantage of scheme members would be eroded by the one-way impact of portability on the scheme. Existing moneys could be rolled over/transferred out of the scheme, but state legislative restrictions would prevent replacement funds from flowing back in via new membership groups.

c) Thirdly, the at-call nature of members' accrued entitlements would force the board to abandon its growth-oriented investment strategy combined with crediting-rate smoothing as a default option for active accumulation benefit members, resulting in an earnings loss of up to one per cent per annum.[12]

10.24 The Committee notes in particular that Queensland Local Government Super is in a unique position through its proposed exclusion from choice of superannuation (should it be introduced) while potentially being simultaneously subject to the portability regime. In addition, the fund's membership is restricted by State legislation, meaning that it cannot seek new members under a portability regime.[13]

10.25 In its supplementary written submission, the Queensland Local Government Superannuation Board indicated that the gazetted regulations do not make any material difference to the substance of the Board's concerns outlined above. Accordingly, the Board requested the exclusion of Queensland Local Government Super from the provisions of the portability regulations through an amendment to

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11 *Submission* 7, Queensland Local Government Superannuation Board, pp. 2-3.

12 *Committee Hansard*, 31 July 2003, p. 44

13 *Committee Hansard*, 31 July 2003, p. 44.

regulation 6.30(2) of the Superannuation Industry (Supervision) Amendment Regulations 2003 (ie. funds to which the Division does not apply).[14]

14 *Submission* 28, Queensland Local Government Superannuation Board, p. 2.

Chapter Eleven

Other Implementation Issues

Introduction

11.1 This chapter examines the following implementation issues in relation to the portability regulations raised during the inquiry:

a) A roll over/transfer protocol;

b) The timing of roll overs/transfers;

c) Suspension or variation of roll overs/transfers;

d) Legal protection for trustees; and

e) The commencement date of the regulations.

A roll over/transfer protocol

11.2 Regulation 6.33 of the Superannuation Industry (Supervision) Amendment Regulations 2003 is the main regulation dealing with the roll over/transfer of withdrawal benefits. It states in part:

> A member of a regulated superannuation fund or an approved deposit fund may, in writing, ask the trustee of the fund to roll over or transfer an amount that is the whole or part of the member's withdrawal benefit.

11.3 In its written submission, ASFA argued that it would assist all parties if this regulation provided more detail of the level of information required to be supplied by the member to the fund. ASFA suggested the possible inclusion of an additional sub-regulation detailing the type of information required such as:

a) The Australian Business Number (ABN) of the destined fund;

b) The amount to be rolled over/transferred out of the fund; and

c) Either the SPIN of the destination fund/product or the member's account number of that fund.[1]

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1 *Submission* 2, ASFA, p. 6.

11.4 This point was also made by IFF in its written submission. It argued that there needs to be a standard industry-wide protocol setting out the data that all superannuation funds need in order to implement a roll over/transfer request. The IFF suggested that currently, some funds delay implementing roll over/transfer requests because they claim to require further information (which in some cases seems designed to cause a member to abandon their request in frustration).[2]

11.5 Similarly, Cbus also argued that a roll over/transfer protocol should be included in the regulations. Such a protocol should define exactly what information is required for a roll over/transfer to occur and establish a standard form approved by the industry regulator to facilitate roll overs/transfers.[3] This point was also made by CPA Australia.[4]

11.6 The Committee also raised the issue of a roll over/transfer protocol with Mr Korchinski from AAS in the hearing on 31 July 2003. Mr Korchinski indicated:

> The whole transfer protocol has been a matter that the industry has looked at for many years. It is conceptually attractive but very difficult to implement. The problem with the implementation is primarily due to the fact that a lot of the transfer processes are computerised—whilst we do have a standard protocol in place, for many of the funds the costs to actually move to that protocol are excessive, and there is no attraction in the short term to offset that cost. It is one of the disappointments within the industry, because in the majority of cases we issue cheques to transfer when there should conceptually be a clearing house approach, much like the way cheque clearing occurs.[5]

11.7 The Committee notes that Mr Silk from IFF,[6] Ms Kelleher from CPA Australia[7] and Mr Noble from Cbus also indicated in the hearing on 1 August 2003 their support for the development of an industry-wide roll over/transfer protocol. Mr Noble stated:

> We believe that, in terms of the practices in the industry and consolidating superannuation accounts, good practice is not exercised by all participants in the industry. We believe that we operate on a basis of professionalism, trying to process rollovers as smoothly and professionally as possible, but we do believe that there are some providers out there who will delay the processing of rollover requests and who ultimately ask for their own forms to be used. When this is done, it creates another obstacle for members

2 *Submission* 4, IFF, p. 2.

3 *Submission* 16, Cbus, p. 5.

4 *Submission* 13, CPA, p. 2.

5 *Committee Hansard*, 31 July 2003, p. 55.

6 *Committee Hansard*, 1 August 2003, p. 6.

7 *Committee Hansard*, 1 August 2003, p. 52.

> because members find it difficult enough to understand the superannuation system without being pushed through another hoop in terms of consolidating their superannuation accounts. We believe that we need some transfer protocols to ensure that we do get a consistency of standards across the industry in terms of rollovers.[8]

The timing of roll overs/transfers

11.8 Under regulation 6.34(3) of the Superannuation Industry (Supervision) Amendment Regulations 2003, it is proposed that subject to certain restraints, if a trustee of a regulated superannuation fund or an approved deposit fund receives a request for a roll over/transfer under regulation 6.33, the trustee must roll over/transfer the amount as soon as practicable, and in any case within 90 days after:

a) Receiving the request; or

b) If the trustee requires further information in relation to the request – receiving the further information; or

c) If there is a suspension under regulations 6.36 or 6.37 – the end of the period of the suspension.

11.9 In its September 2002 consultation paper on portability, Treasury noted that to adopt a longer notification period, such as 12 months, would diminish the effectiveness of the policy in meeting its objectives. In particular, it would reduce the extent to which portability would enhance competition between superannuation providers and, therefore, reduce the pressure on all funds to maintain investment strategies that meet the needs of members. It would also mean that some fund members would be required to keep their benefits in a fund that they did not consider was meeting their needs.[9]

11.10 The Committee notes that a number of parties in their written submissions recommended a shorter roll over/transfer period than 90 days:

- IFF acknowledged that the 90 day requirement will address the issue of deliberate delays by some superannuation funds in meeting a roll over/transfer request, but supported a shorter roll over/transfer period of 45 days following receipt of all necessary information.[10]
- The AIG suggested that the 90 day allowance could ‘possibly even be shortened’;[11]

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8 *Committee Hansard*, 1 August 2003, p. 21.

9 Commonwealth Treasury, *Portability of Superannuation Benefits*, p. 15.

10 *Submission* 4, IFF, p. 2.

11 *Submission* 5, AIG, p. 1.

- The ACTU argued that the 90 day allowance could reasonably be reduced to 30 days.[12]

11.11 However, Cbus supported the 90 day period as appropriate.[13] Similarly, in its written submission, AAS argued that its clients would regard a service level of 90 days as well outside acceptable standards, but indicated that 90 days may be an acceptable minimum standard.[14]

11.12 The Committee also raised this issue in hearings. Mr Korchinski from AAS indicated that 90 days to meet a request from a member for a roll over/transfer would generally be considered poor service, and that it would be reasonable for superannuation providers to meet a more 'reasonable service standard'.[15] In addition, Mr Silk from IFF expressed his belief that a 30 or 45 day period would give superannuation funds sufficient time to act on a request following receipt of appropriate documentation.[16]

Suspension or variation of roll overs/transfers

Regulation 6.36 – Suspension or variation of obligation to roll over/transfer amounts by APRA

11.13 Under regulation 6.36 of the Superannuation Industry (Supervision) Amendment Regulations 2003, APRA may, by notice in writing to the trustee, suspend or vary an obligation on the trustee under regulation 6.34, if APRA believes on reasonable grounds that a roll over/transfer of an amount would have a significant adverse effect on:

a) The financial position of the fund; or

b) The interest of other members of the fund.

11.14 In their written submission, both ASFA and CPA Australia questioned whether the terms 'reasonable grounds' and 'significant adverse effect' require definition either through regulation or a Superannuation Circular issued by APRA prior to the provision coming into effect.

11.15 The Corporate Super Association also argued that it is desirable that information and guidelines be made available about the circumstances under which

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12 *Submission* 10, ACTU, p. 1.

13 *Submission* 16, Cbus, p. 5.

14 *Submission* 18, AAS, p. 3.

15 *Committee Hansard*, 31 July 2003, p. 55.

16 *Committee Hansard*, 1 August 2003, p. 4.

APRA would be likely to exercise its discretion, whether unilaterally or at the request of a fund's trustee (regulation 6.37).[17]

Regulation 6.37 – Suspension or variation of obligation to roll over/transfer amounts by APRA – application by trustee

11.16 Under regulation 6.37 of the Superannuation Industry (Supervision) Amendment Regulations 2003, a trustee may apply to APRA to suspend or vary the trustee's obligation to roll over/transfer an amount under regulation 6.34.

11.17 In its written submission, ASFA argued that there should be some time constraint imposed on trustees wishing to avail themselves of regulation 6.37. ASFA suggested that as the provision stands, a trustee may receive a valid application for a roll over/transfer, but could wait for, say, 80 days, before making an application to the regulator for relief. Although APRA has 30 days to respond under draft Regulation 6.37(5), draft regulation 6.43 would require the trustee to make the payment no later than 90 days after the application for a roll over/transfer.

11.18 Accordingly, ASFA proposed that a time limit, for example 30 days from receiving a request for a roll over/transfer, be imposed on the ability of a trustee to apply to APRA for relief under draft regulation 6.37. This would avoid any conflict that may arise between the requirement to roll over/transfer an amount and seeking and gaining relief due to an inability to pay.[18]

11.19 The Committee notes that this issue remains applicable to the gazetted regulations.

Protection for trustees

11.20 On a related issue, Mr Riordan from the Law Council of Australia noted that regulation 6.34(3) of the Superannuation Industry (Supervision) Amendment Regulations 2003, which requires that a trustee must roll over or transfer an amount within 90 days, does not allow for 'variation' or 'suspension' of that requirement under regulation 6.36 and 6.37. Accordingly, the Council argued that regulation 6.34(3)(c) needs to be amended to include reference to the roll over/transfer having to be accomplished within 90 days after 'notification of the variation under regulations 6.36(2) or 6.37(6).'[19]

11.21 Mr Riordan and the Law Council of Australia in its submission also raised the possibility that under regulation 6.34(3) of the Superannuation Industry (Supervision) Amendment Regulations 2003, a trustee may make an application to APRA under regulation 6.37 for suspension of a transfer, but that APRA may not make a decision

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17 *Submission* 9, Corporate Super Association, p. 6.

18 *Submission* 2, ASFA, p. 7.

19 *Submission* 20, Law Council of Australia, p. 3. *Committee Hansard*, 14 August 2003, p. 2.

within 90 days, placing the trustee in breach of the regulation. Accordingly, the Council argued that some form of protection is required for a trustee who does not receive a response from APRA within the 90 day period.[20]

Legal protection for trustees

11.22 In its written submission, the Law Council of Australia noted that there does not seem to be any legal protection for trustees under the draft regulation where a member rolls over/transfers their savings, but it later turns out they would have been better off staying where they were. The Council noted that in the family law superannuation splitting context, the trustee is expressly protected when it rolls over/transfers an amount in accordance with that regime.[21] Mr Riordan from the Law Council of Australia reiterated this concern in relation to the gazetted regulations in the hearing on 13 August 2003.[22]

11.23 Treasury replied to this matter in its response to questions on notice dated 18 August 2003. Treasury noted that there are already in place a number of protections for trustees:

> a) In particular, section 341 of the SIS Act expressly protects trustees from liability in relation to an act done in fulfilment of an obligation imposed by the SIS Act or SIS Regulations. The obligation to rollover or transfer a benefit under portability is contained in the SIS Regulations and hence would be covered by section 341.
>
> b) Section 310 of the SIS Act also provides protection. This section provides that in civil proceedings against trustees a court has the power to relieve the person of liability if the person acted honestly and having regard to all the circumstances, the person ought fairly to be excused. This defence applies to an action for negligence, default, breach of trust, or breach of duty.

11.24 Given these existing protections in the SIS Act, Treasury submitted that it does not appear that any further protection for trustees is necessary under the regulations.[23]

11.25 The Committee in turn requested the Law Council of Australia to respond to Treasury's position. In its supplementary written submission dated 25 August 2003, the Law Council made the following points:

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20 *Submission* 20, Law Council of Australia, p. 3.

21 *Submission* 20, Law Council of Australia, p. 4.

22 *Committee Hansard*, 13 August 2003, p. 2.

23 Treasury, Response to Questions on Notice, 18 August 2003, p. 1.

a) Section 341 of the SIS Act: The Law Council of Australia argued that section 341 of the SIS Act provides protection to a trustee but is limited to liability for civil proceedings in relation to an act done in the fulfilment of an obligation imposed by the SIS Act or SIS Act Regulations. Accordingly, the Law Council of Australia argued that section 341 provides inadequate protection for trustees on two grounds:

Firstly, the provision can only be used as a defence to an action brought against a trustee rather than a true immunity for the fulfilment of obligations imposed on a trustee in accordance with the SIS Act and SIS Act Regulations.

Secondly, the defence is limited by the fact that it only covers acts which are done in 'fulfilment of an obligation'. This will not cover ancillary acts of a trustee. For example, in the context of the gazetted regulation 6.34, a trustee will only be protected in relation to actions taken to ensure that a member is aware that they may ask the trustee for information regarding the entitlements that the member may have. This will not cover information provided by the trustee pursuant to a request from a member.

b) Section 310 the SIS Act: The Law Council of Australia noted that Section 310 of the SIS Act provides the Courts with the power to grant relief of liability for civil proceedings bought against a superannuation official for official misconduct in the capacity of their role. A court may release a party from such liability where it appears that the official may be liable in respect of a claim and the official has acted honestly and having regard to all the circumstances of the case he or she ought fairly be excused for the official misconduct.

Once again, however, the Law Council of Australia argued that section 310 is inadequate to protect trustees in relation to the gazetted regulations. The Council made three points:

First, as with section 341, the provision grants only a defence to a civil proceeding or potential civil proceeding rather than a true immunity.

Secondly, the power to grant relief is confined to actions for 'official misconduct' which is of no relevance to division 6.5 of the gazetted regulations.

Thirdly, some commentators have questioned the constitutional validity of the provision.

11.26 Given its concerns, the Law Council of Australia advocated in its supplementary submission the inclusion of a specific section in the portability

regulations to protect trustees. That section could be modeled on section 90MZE of the *Family Law Act 1975* along the following lines:

> The trustee of an eligible superannuation plan is not liable for loss or damage suffered by any person because of anything done (or not done) by the trustee in good faith:
>
> a) in relation to any roll over or transfer of a withdrawal benefit under this division; or
>
> b) where the trustee has made an application under regulation 6.37 to APRA to suspend the trustee's obligations to roll over or transfer a withdrawal benefit and APRA has not responded within 90 days; or
>
> c) where the trustee is unable to facilitate a roll over or transfer of withdrawal benefit due to a delay resulting from a request made by APRA for further information in accordance with an application made under regulation 6.37.[24]

11.27 The Committee notes that this proposed section picks up the concerns noted earlier of the Law Council of Australia in relation to the suspension or variation of roll overs/transfers.

Commencement date

11.28 In its written submission, Mercer argued that the introduction of portability will require many funds to implement significant systems changes. In addition, Mercer noted that trustees are currently heavily involved in implementing procedures to cope with the new FSR Act requirements. Furthermore, from early next year, it is likely that trustees will also need to start preparing for the draft APRA licensing arrangements.

11.29 Accordingly, Mercer argued that portability should not commence until at least 12 months after either the regulations have been gazetted or any changes to surcharge legislation and procedures have been finalised. Mercer suggested that the current draft commencement date of 1 July 2004 is unrealistic.[25]

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24 *Submission* 33, Law Council of Australia, pp. 1-2.

25 *Submission* 17, Mercer, p. 7.

Chapter Twelve

Conclusions and Recommendations

Parties to the inquiry

12.1 The Committee notes general support for the principle of portability of superannuation, on the basis that superannuation fund members should have the ability to manage their superannuation.

12.2 However, only two parties to the inquiry outside of Government, namely IFSA and the ABA, supported the specific terms of the gazetted regulations, dated 30 July 2003. IFSA and the ABA argued that consumers should have the right to select where their superannuation funds are invested, and that the best governance standards occur when consumers are informed and freely choose which financial services provider they will trust with their funds.

12.3 The Committee also notes the evidence of Treasury that many funds already provide portability without any significant problems, and that all the new regulations are really doing is extending that same right to a further group of superannuation fund members.

12.4 The great majority of parties to the inquiry opposed the specific terms of the draft or gazetted regulations, or the implementation of the regulations in the current environment. The Committee notes that a broad range of issues was raised. These are examined below.

Roll overs/transfers out of active accounts

12.5 The principal concern expressed by parties making submissions to the inquiry in response to the draft regulations was that they would mandate the right of superannuation fund members to roll over/transfer their superannuation savings out of an active fund (ie one still receiving employer sponsored SG contributions) into an inactive fund. It was argued that this would effectively constitute *de facto* choice of fund, or choice of fund by the back door.

12.6 The Committee notes that this concern still partly holds under the gazetted regulations. The gazetted regulations limit the number of roll overs/transfers out of an active or inactive account to one a year. Nevertheless, such a roll over/transfer out of an active account still effectively amounts to choice of fund. To implement such a measure would pre-empt the legislative intent of the parliament, which has previously rejected choice of fund legislation.

12.7 The Committee believes that the gazetted regulations should be amended to exclude portability out of an active account.

12.8 The Committee believes that an appropriate minimum standard measure of whether an account is active or inactive would be whether the fund received any contributions in the last 12 months. This would be sufficient time to pick up most cyclical or casual jobs. Clearly this would not apply if the employee had changed employment and was receiving mandated SG payment in another fund.

Portability, choice and parliamentary scrutiny

12.9 Many parties to the inquiry argued that the portability regulations should not operate independently of choice legislation. It was noted to the Committee that the Government has previously directly associated portability with choice.

12.10 The Committee believes that it would have been preferable to consider the portability regulations alongside choice of fund legislation. Indeed the Committee made this point in its previous report on choice tabled in November 2002, entitled *Provisions of the Superannuation Legislation Amendment (Choice of Superannuation Funds) Bill 2002*. However, the Committee accepts that portability and choice can stand alone where there is not portability out of an active account.

12.11 The Committee notes that the Government intends to introduce a revised choice bill in the spring sittings of Parliament. This was announced by the Assistant Treasurer, Senator Coonan, in a media release on 25 May 2003.

Superannuation account numbers

12.12 In the March quarter 2003, Australia's 9 million fund members held between them 25.5 million superannuation accounts – an average of 2.8 accounts per member. The Committee recognises the desirability of consolidating some of these accounts.

12.13 However, a number of parties to the inquiry argued that roll overs/transfers out of active superannuation accounts, as permitted under the gazetted regulations, would simply lead to a proliferation of superannuation accounts, rather than the anticipated consolidation of accounts.

12.14 The Committee accepts that the ability of fund members to roll over/transfer out of an active account into a new account would simply increase account numbers and churning. This holds true despite the change in the gazetted regulations to restrict roll overs/transfers out of active accounts to one a year.

12.15 At the same time, however, although it was not broadly canvassed by parties to the inquiry, the Committee accepts that the gazetted regulations provide an opportunity to some fund members to consolidate inactive fund accounts where at present they may be prevented from doing so.

Financial disclosure standards in Australia

12.16 The Committee believes that adequate and consistent financial disclosure by superannuation funds, including the provision of information such as a member's withdrawal benefit, investment strategies, rates of return, fees, charges and expenses, is essential if portability is to be introduced successfully in Australia.

12.17 Disclosure requirements for superannuation funds are now provided under the Corporations Act, as amended by the FSR Act, which commenced on 11 March 2002 (subject to certain transitional arrangements).

12.18 During the inquiry, a number of parties argued that portability should be delayed until the effectiveness of the FSR Act can be gauged. By contrast, other parties argued that the new FSR Act represents world's best consumer protection and should be given an opportunity to prove its effectiveness.

12.19 The Committee also notes that ASIC has recently released its new model for product disclosure statements. ASIC's model aims to address issues such as:

- The use of common terms;
- Standardised descriptions;
- Disclosure of the purpose of particular fees;
- Improved disclosure of adviser remuneration; and
- Transparency of fees.[1]

12.20 The Committee notes, however, evidence that further refinement of product disclosure statements is required by ASIC to address issues such as expressing fees in dollar terms, disclosure of so-called 'soft-dollar perks', and the impact that fees and charges will have on the future returns of a fund.

12.21 The Committee believes that the financial disclosure environment in Australia will continue to improve with the full implementation of the FSR Act and further refinement of the Product Disclosure Statements by ASIC.

12.22 The Committee also notes that in the gazetted regulations, the Government introduced regulation 6.34(2) which requires that, prior to making a roll over/transfer, a trustee must be satisfied that the member is aware of his or her right to receive additional information on the effect of the roll over/transfer (eg. impact of fees or insurance cover) and is satisfied that the member does not require such information.

12.23 The provisions of regulation 6.34(2) came under considerable scrutiny during the inquiry. It was suggested that:

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1 ASIC Media Release, 'ASIC Releases Fee Disclosure Model', 5 August 2003.

a) It is unclear how this mechanism is meant to work, and that it may potentially become a 'rubber stamp exercise'.

b) It may expose trustees and employers to subsequent legal action where a member makes a poor investment decision and later tries to sue the trustee or employer.

12.24 Accordingly, the Committee believes that regulation 6.34(2) of the Superannuation Industry (Supervision) Amendment Regulations 2003 (No.4) should be revisited to clarify its proposed operation and to protect trustees and employers from any retrospective legal action.

Financial education standards in Australia

12.25 The Committee notes that as with financial disclosure standards, various parties to the inquiry expressed concern about financial education standards in Australia. In particular, it was suggested that fund members lack sufficient education to be able to compare superannuation products in order to make an informed choice about portability of superannuation.

12.26 The Committee acknowledges this problem. In the Committee's opinion, there are no short-term solutions to the general lack of education in the Australian population in relation to superannuation and retirement savings. Any change is likely to be generational, beginning with the inclusion of financial education in the curriculum in schools. However, more immediately, financial education needs to be provided in universities, workplaces and by funds themselves.

12.27 The Committee notes that in its September 2002 consultation paper, Treasury indicated that it would conduct an education campaign prior to the commencement of the portability regulations. The campaign would be designed to meet the information needs of both fund trustees and fund members.

12.28 In this regard, the Committee notes that the $28.7 million allocated by the Government over four years in the 2002-2003 Budget is to fund an education campaign targeting both choice of fund and portability.

12.29 The Committee acknowledges that such an education campaign cannot possibly reach every individual in Australia. Nevertheless, the Committee notes that many superannuants seek outside education and advice on financial matters, and anticipates that this will only increase in the future with the conduct of an appropriate education campaign.

Life insurance arrangements

12.30 The Committee notes that the gazetted regulations, which allow trustees to require members to leave a balance of up to $5,000 behind in a fund, effectively address the concern that individuals would not have sufficient funds in their superannuation account to maintain their insurance coverage.

The superannuation surcharge

12.31 The Committee was presented with strong evidence that the portability regulations, especially the implementation of partial fund roll overs/transfers, would involve major difficulties for funds trustees and financial service providers administering the superannuation surcharge. In particular, it was argued that the portability regulations would introduce major difficulties in:

a) Determining how much of a rolled over/transferred amount related to surchargeable contributions for the current year. For example, if a partial roll over/transfer is made, the difficulty would be to determine how much of the surchargeable contributions for that year related to the partial withdrawal, and how much related to previous years.

b) Handling surcharge assessments. It was argued that there will be considerable disagreement as to whether a fund is still 'the holder of the contributions' for surcharge assessment purposes, as a surcharge assessment may relate to contributions made in an earlier year which has already been paid out of the fund.

12.32 In response to these issues, the Committee was reassured by evidence from officers of the ATO that the new regulations would not involve any significant further difficulties, although there may potentially be more roll overs/transfers, involving greater costs.

12.33 That said, the Committee accepts that this is a very difficult issue, and that the impact on some trustees and financial service providers of meeting superannuation surcharge issues may be disproportionate to that on others. The Committee believes that the Government should consult further with the industry on this matter.

Multiple/partial roll over/transfer costs

12.34 During the inquiry, a number of parties raised concern about the impact that unlimited and partial roll overs/transfers, as proposed in the draft regulations, would have on the administration and hence costs of funds. It was suggested that members could begin to treat superannuation interests like a bank account.

12.35 As indicated in Chapter One, these concerns have been partially redressed in the gazetted regulations through a move to minimise roll overs/transfers to one a year. Nevertheless, it is clear that funds face additional costs under the regulations.

12.36 In relation to partial roll over/transfer, the Committee believes that where the cost to the fund is fully recoverable through an appropriate exit fee, there should be no restriction on partial roll overs/transfers. The advantage of partial roll overs/transfers is that they give members the opportunity to manage risk by diversifying their accounts.

Exit fees

12.37 The Committee notes that the issue of exit fees continues to be very controversial, with considerable disagreement amongst parties as to the nature, level and applicability of exit fees.

12.38 On the one hand, the Committee was presented with evidence by IFF and Cbus that high exit fees are widespread in the superannuation industry and constitute a significant barrier to portability out of an account.

12.39 On the other hand, IFSA, the FPA and the ABA presented evidence that high exit fees are confined to superannuation products that were offered during the 1980s by the life insurance industry, and that such products now constitute less than 5 per cent of all retail and master trust funds under management.

12.40 Given this disagreement about the real impediment to portability that exit fees provide, there remains considerable debate whether a cap or even ban should be placed on exit fees.

12.41 A large number of parties supported a cap on exit fees at a fixed dollar amount, set at a level sufficient to cover actual administrative expenses to a fund from a roll over/transfer. Such a cap would need to be prospective rather than retrospective.

12.42 In response to this argument for a fee cap, IFSA suggested that regulation of exit fees would be counter productive from a competition, choice and consumer design perspective. If a cap was placed on fees, IFSA argued that fees would tend to rise to match the level of the cap.

12.43 The Committee believes that future exit fees should be limited to the reasonable administrative cost and redemption cost of a roll over/transfer. The Committee notes that in its September 2002 consultation paper, the Government left open the option of regulating exit fees.

12.44 Although not raised during the conduct of the inquiry, the Committee also believes that the Government should investigate whether there should be a greater role for the Superannuation Complaints Tribunal in dealing with complaints about fees and charges. Currently, the tribunal cannot generally deal with a complaint that fees and charges are too high, although it may be able to deal with a complaint that fees and charges were not disclosed or that misrepresentations were made about the existence or level of fees and charges.

Fund investments and liquidity

12.45 The Committee notes concern that higher levels of churning between funds under the portability regulations would require funds to retain more liquid assets so as to be able to meet their liquidity obligations under the SIS Act. In turn, forcing funds to maintain more liquid assets would lead to lower long-term average returns.

12.46 In response, it was argued by IFSA that long-term investments are readily available and redeemable on the stock market, and that portability would have little or no impact on fund returns.

12.47 The Committee does not regard the impact of the portability regulations on fund liquidity and investment returns as a reason to delay the introduction of the regulations. However, the Committee acknowledges that more frequent roll overs/transfers could have a modest impact on fund liquidity and hence returns.

12.48 The Committee endorses the evidence of APRA that trustees will need to review fund liquidity and their risk profile from 1 July 2004.

Commission-based selling

12.49 The Committee notes concerns that the portability regulations could increase the likelihood of fund members being persuaded by financial advisers to move their savings around either once or repeatedly, the principal advantage of which would accrue to the advisers in the form of commissions. To prevent this, various parties recommended a ban on commission-based roll overs/transfers of mandated employer superannuation contributions.

12.50 In response to these concerns, the FPA noted that Section 947D of the new FSR Act makes it clear that the Government will not tolerate churning of fund members by financial advisers. The Committee is also encouraged by the FPA's new Professional Partner Program aimed at 'raising the bar' in relation to professional standards in the financial planning community.

12.51 The Committee has some concerns in regard to commission-based selling where it impacts on compulsory SG funds. In its previous report entitled *Planning for Retirement*, the Committee indicated its opinion that the mechanisms for remunerating financial planners need reform to implement a more direct relationship between the amount of work performed and the fee charged. The Committee further recommended that the Productivity Commission investigate the remuneration arrangements for financial planners.

12.52 The Committee believes that commission-based selling should be re-examined by the Government following the outcome of the Productivity Commission investigation.

Not-for-profit funds

12.53 The Committee notes the concerns expressed by the Corporate Super Association, AAS and SOS that the portability regulations would lead to a one-way flow of funds out of not-for-profit employer-sponsored superannuation funds into retail funds. This is because retail funds can promote themselves to the public and invite membership whereas not-for-profit funds do not seek roll overs/transfers from the general public.

12.54 The Committee recognises the concerns of not-for profit funds, but does not believe that the solution to this problem is to prevent portability. Rather, as indicated in the Committee's previous report entitled *Planning for Retirement*, the imperative is to ensure that financial planners provide independent and unbiased advice by removing any commercial advantage from the provision of that advice.

Defined benefit schemes

12.55 The Committee notes the issue raised by Watson Wyatt that it is quite common for a defined benefit fund in Australia to have a benefit design that provides:

a) On resignation prior to the attainment of a specified period of service or age, a benefit that is accumulative in nature (eg. a benefit that is the sum of a member account and a company account, or a benefit that is expressed as a multiple of member account); or

b) On attainment of the specified period of service or age, a benefit that is defined benefit in nature (eg. a benefit based on a certain factor multiplied by years of service multiplied by average salary).

12.56 Watson Wyatt submitted that such an interest should be classified as a defined benefit component for the purposes of regulation 6.30(2)(c), thus excluding such benefits from the provisions of the Superannuation Industry (Supervision) Amendment Regulations 2003.

12.57 The Committee believes that the Government should examine this issue to determine whether any further modifications to regulation 6.30(2)(c) of the Superannuation Industry (Supervision) Amendment Regulations 2003 is warranted.

Unfunded Public Sector Superannuation Schemes

12.58 The Committee notes the concerns of the Government Employees Superannuation Board of Western Australia in relation to the definition of unfunded public sector superannuation schemes in the *Superannuation Contributions Tax (Assessment and Collection) Regulations 1997.* Put simply, the 1997 regulations refer to two repealed Western Australian Acts.

12.59 The Committee believes that the *Superannuation Contributions Tax (Assessment and Collection) Regulations 1997* should be amended to reflect current legislative circumstances in WA. The Government should also take steps to consolidate the terms used to refer to superannuation schemes administered under Commonwealth, State or Territory Law.

The Queensland Local Government Superannuation Scheme

12.60 The Committee notes that the Queensland Local Government Super is in a unique position through its proposed exclusion from federal choice of superannuation

legislation (should it be enacted), while potentially being simultaneously subject to the portability regime.

12.61 The Committee believes that the Queensland Local Government Super, and any other funds in a similar position, should be excluded from the provisions of the Superannuation Industry (Supervision) Amendment Regulations 2003.

A roll over/transfer protocol

12.62 The Committee notes considerable support for the development and inclusion in the regulations of a roll over/transfer protocol to help facilitate roll overs/transfers. ASFA suggested the possible inclusion in the regulations of an additional sub-regulation detailing the type of information required, such as:

a) The ABN of the destined fund;

b) The amount to be rolled over/transferred out of the fund; and

c) Either the SPIN of the destination fund/product or the member's account number of that fund.[2]

12.63 The Committee supports the development and inclusion in the regulations of a roll over/transfer protocol. That said, the Committee notes that a roll over/transfer protocol has been a matter that the industry has looked at for many years, but which has proved very difficult to implement for some funds.

The timing of roll overs/transfers

12.64 The Committee notes arguments that the 90 day roll over/transfer period under regulation 6.34(3) of the Superannuation Industry (Supervision) Amendment Regulations 2003 is excessively generous, and that a shorter roll over/transfer period could be enforced. However, the Committee believes that while a 90 day roll over/transfer would generally be considered as outside normal standards, it nevertheless represents an acceptable minimum standard.

Suspension or variation of roll overs/transfer

12.65 The Committee believes that the Government should investigate whether there needs to be:

a) Definition of the terms 'reasonable grounds' and 'significant adverse effect' under regulation 6.36 of the Superannuation Industry (Supervision) Amendment Regulations 2003.

b) A time limit, for example within 30 days of receiving a request for a roll over/transfer, on the ability of a trustee to apply to APRA for

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2 *Submission* 2, ASFA, p. 6.

relief under regulation 6.37. This would avoid any conflict that may arise between the requirement to roll over/transfer an amount and seeking and gaining relief due to an inability to pay.

12.66 The Committee also endorses the concerns of the Law Council of Australia that:

a) Regulation 6.34(3) does not allow for 'variation' or 'suspension' of a transfer under regulations 6.36 and 6.37.

b) A trustee may make an application to APRA under regulation 6.37 for suspension of a transfer under regulation 6.34(3), but APRA may not make a decision within 90 days, placing the trustee in breach of the regulation.

Legal protection for trustees

12.67 The Committee endorses the concern of the Law Council of Australia that trustees should be provided with legal protection under the portability regulations to make it clear that if a roll over/transfer occurs in accordance with the regulations, the member bears the risk.

12.68 Accordingly, the Committee believes that the portability regulations should include a section giving specific legal protection to trustees, in accordance with the model outlined by the Law Council of Australia in paragraph 11.26.

Summary

12.69 <u>The Committee supports the principle of portability, and the ability of individuals to consolidate their superannuation accounts. In particular, the Committee supports giving individuals the ability to consolidate an inactive superannuation account into either an active account or another inactive account. Such a measure, accompanied by a targeted education campaign following the introduction of portability, would achieve a reduction in superannuation account numbers in Australia.</u>

12.70 However, the Committee believes that the portability regulations, by extending portability to active accounts, raise an issue which is better dealt with through choice of funds legislation on the grounds of efficiency and consumer protection. There may also be concerns where a person's death benefit is significantly greater than the member's account balance. The Committee is also concerned that portability out of active superannuation accounts could lead to an increase in superannuation account numbers in Australia due to the need to maintain multiple accounts.

12.71 Accordingly, the Committee believes that the Government should revise the Superannuation Industry (Supervision) Amendment Regulations 2003 (No. 4) and the

Retirement Savings Accounts Amendment Regulations 2003 (No. 2) to prohibit roll overs/transfers out of an active superannuation account into an inactive account.

12.72 The Committee notes that the Superannuation Industry (Supervision) Amendment Regulations 2003 (No. 4) and the Retirement Savings Accounts Amendment Regulations 2003 (No. 2) are not due to come into force until 1 July 2004.

Recommendation 1

The Committee recommends that the Government prior to 1 July 2004 revise the Superannuation Industry (Supervision) Amendment Regulations 2003 (No. 4) and the Retirement Savings Accounts Amendment Regulations 2003 (No. 2) to prohibit roll overs/transfers out of an active superannuation account.

12.73 The Committee also believes that when revising the Superannuation Industry (Supervision) Amendment Regulations 2003 (No. 4) and the Retirement Savings Accounts Amendment Regulations 2003 (No. 2), the Government should:

- Revise regulation 6.34(2) of the Superannuation Industry (Supervision) Amendment Regulations 2003 (No.4) relating to disclosure to clarify its proposed operation and to protect trustees and employers from any retrospective legal action;
- Revise regulation 6.30(2)(c) of the Superannuation Industry (Supervision) Amendment Regulations 2003 (No.4) to exclude defined benefit schemes from the provisions of the regulation where the member's current entitlement is in accumulation or partially vested form;
- Exclude Queensland Local Government Super (and any other funds in a similar position) from the operation of the Superannuation Industry (Supervision) Amendment Regulations 2003 (No.4) due to the particular nature of the scheme under state legislation;
- Include a roll over/transfer protocol, based on consultation with the industry, to help facilitate roll overs/transfers;
- Examine the timing, suspension and variation of roll overs/transfers under regulations 6.34, 6.36 and 6.37 of the Superannuation Industry (Supervision) Amendment Regulations 2003 (No.4); and
- Include a section giving specific legal protection to trustees, in accordance with the model outlined by the Law Council of Australia in paragraph 11.26.

Recommendation 2

The Committee recommends that when revising the Superannuation Industry (Supervision) Amendment Regulations 2003 (No. 4) and the Retirement Savings Accounts Amendment Regulations 2003 (No. 2), the Government should also address the issues raised in Paragraph 12.73.

12.74 The Committee also notes that the introduction of portability of superannuation in Australia would be further facilitated by:

- The commencement of the education campaign on choice and portability when the portability regulations come into effect using the $28.7 million allocated by the Government over four years in the 2002-2003 Budget;
- Further refinement of product disclosure statements by ASIC;
- Limiting future exit fees to the reasonable administrative cost and redemption cost of a roll over/transfer;
- Further consultation with the industry on the handling of surchargeable contributions;
- An extension to the role for the Superannuation Complaints Tribunal in dealing with complaints about fees and charges; and
- Revising the *Superannuation Contributions Tax (Assessment and Collection) Regulations 1997* to reflect current legislative circumstances in WA and to consolidate the terms used to refer to superannuation schemes administered under Commonwealth, State or Territory Law.

Recommendation 3

The Committee recommends that the Government prepare for the introduction of portability and choice by addressing the issues raised in paragraph 12.74. In particular, the Committee believes that when the portability regulations come into effect, the Government should commence its education campaign using the $28.7 million allocated by the Government over four years in the 2002-2003 Budget.

12.75 Labor and Democrat Senators note that they will move to disallow the Superannuation Industry (Supervision) Amendment Regulations 2003 (No. 4) and the Retirement Savings Accounts Amendment Regulations 2003 (No. 2) in the Senate if the Government does not support the recommendations in this report.

Senator John Watson
Committee Chair

Statement on the Gazettal of the Regulations

The Committee wishes to comment on the gazettal of the Superannuation Industry (Supervision) Amendment Regulations 2003 and the Retirement Savings Accounts Amendment Regulations 2003 on 30 July 2003, the day before the Committee's first public hearing on this matter on 31 July 2003.

This action placed members of the Committee in a very difficult and embarrassing position during the public hearings. Furthermore, witnesses appearing before the Committee were obliged to attempt to reconsider their evidence and submissions to the Committee at very short notice. In some instances, this simply was not possible.

The Committee believes that there was ample scope prior to 30 July 2003 for the Treasury and the Government to inform the Committee of the impending gazettal of the regulations. Their failure to do so, despite ample opportunity, made the conduct of this inquiry by the Committee significantly more difficult than it should have been.

Additional Comments by Labor Senators

Introduction

13.1 Labor endorses the major conclusions of the Committee's report into the draft Superannuation Industry (Supervision) Amendment Regulations 2003 and the draft Retirement Savings Accounts Amendment Regulations ("the portability regulations"), and indeed strongly endorses the report's recommendation that the draft regulations be amended to prohibit transfers of funds from active accounts.

13.2 Nonetheless Labor believes there are a number of other issues that need to be addressed before the regulations can be approved.

Portability and Choice

13.3 A major point raised in the report but not adequately addressed in the recommendations is the connection between portability and choice of fund. A substantial number of submissions to the Committee raised the point that the portability regulations, as presently worded, amounted to the introduction of a 'de facto' choice regime. Labor agrees with this view.

13.4 Labor believes that the portability regulations should only be introduced together with a 'safe' choice regime. Given that portability from inactive accounts is generally available to most fund members, Labor can see no need for the proposed regulations in the absence of an established choice regime.

13.5 Labor has stated clearly that it will support a safe choice regime that contains strong protections and safeguards to protect consumers. Consequently, it expects the same protections and safeguards to be in place before it will accept a portability regime that leaves the consumer open to exploitation by the more aggressive elements of the financial services industry.

13.6 The issues that Labor believes need to be adequately addressed before the introduction of a choice regime, including one introduced under the guise of portability include:

a) Consolidation of multiple accounts and costs to funds;

b) Education and disclosure;

c) Fees, charges and commissions; and

d) Death and disability insurance.

Consolidation of Multiple Accounts and the Costs to Funds

13.7 At present it is estimated that there are 25 million superannuation funds established for 9 million fund members. This is clearly inefficient for both the funds, through the costs of maintaining small balances, and the fund member through multiple administration fees.

13.8 Labor fully supports the concept of consolidation of multiple accounts but believes that the proposed portability regulations will not assist. Portability, except from active accounts, is generally available under the existing rules, yet most fund members fail to take up the opportunity.

13.9 Further, the evidence suggests that if the proposed portability regulations were implemented there would be an increase in the numbers of accounts as a fund member may move funds from a single active account to multiple accounts.

13.10 Given that the proposed regulations do not adequately address the issue of multiple accounts and will more likely result in an increase in account numbers, Labor suggests that the implementation of a system that automatically consolidates accounts is necessary. Consolidation from inactive accounts into the most current active account, or where there is no active account, into the most recent inactive account is Labor's preferred model, with the ability of the fund member to opt out of the consolidation process.

13.11 Automatic consolidation would also contribute toward a reduction of the costs of administration of funds, reducing the number of small accounts, and the consequent expense of maintaining those accounts. It would also avoid the pitfalls of a free-for-all portability regime, with the risk of multiple rollovers and the consequential increased costs for superannuation funds in administration and investment management.

Education and Disclosure

13.12 The proposed portability regulations allowing fund members to transfer account balances at will leaves many at the mercy of the financial advising industry. This is a major problem in the light of the most recent survey information available on the levels of consumer knowledge of financial matters, in particular, superannuation (The ANZ Financial Literacy Survey) and the professional and ethical standards of financial planners (The ASIC/ACA Shadow Shopping Survey of Financial Planners).

13.13 Labor believes that the introduction of any portability regulations or choice legislation must be accompanied by a comprehensive and aggressive financial literacy education campaign carried out by the Government in consultation with the financial services industry. Great care must be taken to ensure that any education provided to the public is balanced information and not marketing disguised as education.

13.14 There is an argument that with the advent of the new disclosure rules, consumers will be able to make educated comparisons and decisions about financial

investments, including choosing superannuation products. There is little doubt that improved disclosure, particularly of fees and charges is a major step forward, but like education, disclosure alone is not the answer. For disclosure to be effective it needs to be clear and in a form that makes a comparison between different products possible.

13.15 The introduction of both portability and choice will open consumers up to the high-pressure selling environment of the financial services industry. Even with a comprehensive education program and better disclosure many consumers will remain ill equipped to deal with marketing and sales pressure, disguised as financial advice. This means that to ensure that consumers receive fair and efficient advice, the quality of financial advice must also be dramatically improved on current standards.

Fees, Charges and Commissions

13.16 The fees, charges and commissions on superannuation products remain an on-going concern to Labor. In the context of portability, exit fees are a particular concern as high exit fees effectively operate as a barrier to both portability and choice.

13.17 Portability of superannuation accounts becomes a farce when fees up to 95 per cent of the fund balance can be charged when a member seeks to transfer funds to another account. Taking account of this Labor is of the view that exit fees in their current form must be prohibited and replaced with an administration fee calculated to cover the costs of the administration of a rollover or transfer to another fund.

13.18 Commissions on superannuation guarantee ("SG") contributions are also a concern in the context of portability. There is a risk that some less scrupulous financial adviser will be motivated not by the interests of their client, but by the commissions received for the products they recommend. This will be compounded by the fact that only very financially literate consumers will be able to accurately estimate the real cost of a commission.

13.19 Labor believes that, as the SG is a form of compulsory saving, it must be protected from erosion by costs other than those necessary to administer the fund and its investments. It believes therefore that commissions should be banned on products purchased with SG contributions.

Death and Disability Insurance Cover

13.20 Serious concerns were raised about the implication of the portability regulations and insurance cover provided by many funds. Concerns included:

- The fear that insurance cover provided by many funds, which is generally less costly, could be withdrawn or become more costly; and
- That some members, ignorant of their true insurance entitlements, may transfer to a fund that does not provide comparable insurance benefits.

13.21 Labor believes that these death and disability insurance issues must be firmly addressed before any portability arrangements can be supported.

Conclusion

13.22 Labor believes that the portability regulations must be amended to:

- Prohibit transfers from active superannuation accounts;
- Provide for the automatic consolidation of inactive accounts into the last active account, or where there is no active account, the most recent inactive account;
- Provide for simple, standard, comparable and enforceable disclosure of all fees and charges;
- Include provisions for the funding of an extensive public education campaign on the introduction of any portability or choice regime;
- Include a ban on exit fees and allow funds instead to charge an administrative fee sufficient to cover the reasonable administrative costs of the rollover or transfer;
- Ban commissions on superannuation products purchased with SG contributions; and
- Ensure that fund member insurance entitlements are adequately protected.

13.23 Unless the amendments are made Labor recommends that the regulations be disallowed.

Senator the Hon Nick Sherry

Senator Geoffrey Buckland

Senator Penny Wong

Appendix One

Submissions

1 LG Super
2 Association of Superannuation Funds of Australia
3 Government Employees Superannuation Board of Western Australia
4 Industry Funds Forum
5 Australian Industry Group
6 Motor Trades Association of Australia Superannuation Fund
7 LG Super (Supplementary Submission)
8 Superpartners Pty Ltd
9 Corporate Super Association
10 Australian Council of Trade Unions
11 Australian Institute of Superannuation Trustees
12 Watson Wyatt Worldwide
13 CPA Australia
14 Australian Prudential Regulation Authority
15 Institute of Actuaries of Australia
16 Cbus
17 Mercer Human Resource Consulting
18 Australian Administration Services
19 Society of Superannuants
20 Law Council of Australia
21 Investment and Financial Services Association Ltd
22 The Institute of Chartered Accountants in Australia

23 Taxpayers Australia Inc

24 Financial Planning Association of Australia Limited

25 The Treasury

26 Association of Superannuation Funds of Australia (Supplementary Submission)

27 Watson Wyatt Worldwide (Supplementary Submission)

28 LG Super (Supplementary Submission)

29 Australian Bankers' Association

30 Investment and Financial Services Association Ltd (Supplementary Submission)

31 Industry Funds Forum (Supplementary Submission)

32 Australian Consumers' Association

33 Law Council of Australia (Supplementary Submission)

Appendix Two

Public Hearings

Thursday 31 July 2003, Sydney

Motor Trades Association of Australia Superannuation Fund

Mr Paul Watson, General Manager Superannuation

Association of Superannuation Funds of Australia

Dr Michaela Anderson, Director, Policy and Research

Mr Robert Hodge, Senior Policy Adviser

Australian Institute of Superannuation Trustees

The Hon. Susan Ryan, President

Mr Ian Robertson, Secretary

Investment and Financial Services Association Ltd

Mr Richard Gilbert, Chief Executive Officer

Ms Jo-Anne Bloch, Deputy Chief Executive Officer

Mr Bill Stanhope, Senior Policy Manager

Watson Wyatt Worldwide

Mr Garry Fraser, Principal

Mr Bradford Jeffrey, Head, Superannuation Consulting (Sydney)

Queensland Local Government Superannuation Board (LG Super)

Mr Peter Smith, Chief Executive Officer

Mr John Carpendale, Deputy Chief Executive Officer

Australian Administration Services

Mr Stuart Korchinski, Chief Executive Officer

Mr John Holland, Compliance Officer

Mr Derek Abrahams, Consultant, Professional Financial Solutions

Mr Martin Fitzpatrick, Consultant, Professional Financial Solutions

Financial Planning Association of Australia Ltd

Mr Con Hristodoulidis, National Manager, Policy and Government Relations

Society of Superannuants

Captain Ian Woods, President

Mr Kash Gillies, Secretary

Friday, 1 August 2003, Melbourne

Industry Funds Forum

Mr Ian Silk, Convenor

Superpartners Pty Ltd

Ms Fiona Galbraith, Manager, Compliance

Cbus

Ms Helen Hewett, Fund Secretary

Mr Gordon Noble, Employer Coordinator

Mercer Human Resource Consulting Pty Ltd

Mr John Ward, Manager Research and Information

Corporate Super Association

Mr Nic Brookes, Chief Executive

Mrs Elizabeth Goddard, Head of Research

Institute of Actuaries of Australia

Mr Paul Shallue, Member, Superannuation and Employee Benefits Practice Committee and Chairman, Superannuation and Employee Benefits Practice Committee Legislation

ACTU

Ms Linda Rubinstein, Senior Industrial Officer

CPA Australia

Ms Noelle Kelleher, Member, Superannuation Centre of Excellence

Wednesday, 13 August 2003, Canberra

Law Council of Australia

Mr Gary Riordan, Member, Superannuation Committee

Australian Taxation Office

Mr Mark Jackson, Deputy Commissioner, Superannuation

Mr Chris Casey, Assistant Commissioner, Superannuation

Department of the Treasury

Mr Nigel Murray, Manager, Superannuation, Retirement and Savings Division

Mr Michael Rosser, Manager, Investor Protection Unit, Corporations and Financial Services Division

Mr John Riley, Analyst, Superannuation, Retirement and Savings Division

Mr Brett Wilesmith, Analyst, Corporations and Financial Services Division

Australian Prudential Regulation Authority

Mr Greg Brunner, General Manager, Policy Development

Appendix Three

Tabled Documents

Friday 1 August 2003

Table of exit fees from selected superannuation funds tabled by Mr Ian Silk, Industry Funds Forum (see **Appendix Seven**).

Appendix Four

List of Committee Reports 1991 - 2003

Reports and papers of the previous Select Committees on Superannuation (1991-1998)

- *Super System Survey* - A Background Paper on Retirement Income Arrangements in Twenty-one Countries (December 1991)
- First Report of the Senate Select Committee on Superannuation - *Safeguarding Super* - the Regulation of Superannuation (June 1992)
- Second Report of the Senate Select Committee on Superannuation - *Super Guarantee Bills* (June 1992)
- *Super Charges* - An Issues Paper on Fees, Commissions, Charges and Disclosure in the Superannuation Industry (August 1992)
- Third Report of the Senate Select Committee on Superannuation - *Super and the Financial System* (October 1992)
- *Proceedings of the Super Consumer Seminar*, 4 November 1992 (November 1992)
- Fourth Report of the Senate Select Committee on Superannuation - *Super - Fiscal and Social Links* (December 1992)
- Papers relating to the Byrnwood Ltd, WA Superannuation Fund, 25 March 1992; Interim Report on Fees, Charges and Commissions in the Life Insurance Industry, 3 June 1992 (February 1993)
- Fifth Report of the Senate Select Committee on Superannuation - *Super Supervisory Levy* (May 1993)
- Sixth Report of the Senate Select Committee on Superannuation - *Super - Fees, Charges and Commissions* (June 1993)
- Seventh Report of the Senate Select Committee on Superannuation - *Super Inquiry Overview* (June 1993)
- Eighth Report of the Senate Select Committee on Superannuation - *Inquiry into the Queensland Professional Officers Association Superannuation Fund* (August 1993)

- Ninth Report of the Senate Select Committee on Superannuation - *Super Supervision Bills* (October 1993)
- Tenth Report of the Senate Select Committee on Superannuation - *Super Complaints Tribunal* (December 1993)
- Eleventh Report of the Senate Select Committee on Superannuation - *Privilege Matter Involving Mr Kevin Lindeberg and Mr Des O'Neill* (December 1993)
- A Preliminary Paper Prepared by the Senate Select Committee on Superannuation for the Minister for Social Security, *Options for Allocated Pensions Within the Retirement Incomes System* (March 1994)
- Twelfth Report of the Senate Select Committee on Superannuation - *Super for Housing* (May 1994)
- Thirteenth Report of the Senate Select Committee on Superannuation - *Super Regs I* (August 1994)
- Fourteenth Report of the Senate Select Committee on Superannuation - *Super Regs II* (November 1994)
- Fifteenth Report of the Senate Select Committee on Superannuation - *Super Guarantee - Its Track Record* (February 1995)
- Sixteenth Report of the Senate Select Committee on Superannuation - *Allocated Pensions* (June 1995)
- Seventeenth Report of the Senate Select Committee on Superannuation - *Super and Broken Work Patterns* (November 1995)
- Eighteenth Report of the Senate Select Committee on Superannuation - *Review of the Superannuation Complaints Tribunal* (April 1996)
- Nineteenth Report of the Senate Select Committee on Superannuation - *Reserve Bank Officers' Super Fund* (June 1996)
- Twentieth Report of the Senate Select Committee on Superannuation - *Provisions of the Social Security Legislation Amendment (Further Budget and Other Measures) Bill 1996 - Schedule 1* (November 1996)
- Twenty-first Report of the Senate Select Committee on Superannuation - *Investment of Australia's Superannuation Savings* (December 1996)
- Twenty-second Report of the Senate Select Committee on Superannuation - *Retirement Savings Accounts Legislation* (March 1997)
- Twenty-third Report of the Senate Select Committee on Superannuation - *Superannuation Surcharge Legislation* (March 1997)

- Twenty-fourth Report of the Senate Select Committee on Superannuation - *Schedules 1, 9 & 10 of Taxation Laws Amendment Bill (No. 3) 1997* (June 1997)

- Twenty-fifth Report of the Senate Select Committee on Superannuation - *The Parliamentary Contributory Superannuation Scheme & the Judges' Pension Scheme* (September 1997)

- Twenty-sixth Report of the Senate Select Committee on Superannuation - *Super - Restrictions on Early Access: Small Superannuation Accounts Amendment Bill 1997 and related terms of reference* (September 1997)

- Twenty-seventh Report of the Senate Select Committee on Superannuation - *Superannuation Contributions Tax Amendment Bills* (November 1997)

- *Super Taxing* - An information paper on the Taxation of Superannuation and related matters (February 1998)

- Twenty-eighth Report of the Senate Select Committee on Superannuation – *Choice of Fund* (March 1998)

- Twenty-ninth Report of the Senate Select Committee on Superannuation - *Superannuation Legislation (Commonwealth Employment) Repeal and Amendment Bill 1997, Commonwealth Superannuation Board Bill 1997, Superannuation Legislation (Commonwealth Employment - Saving and Transitional Provisions) Bill 1997* (April 1998)

- Thirtieth Report of the Senate Select Committee on Superannuation - *Workplace Relations Amendment (Superannuation) Bill 1997* (May 1998)

- Thirty-first Report of the Senate Select Committee on Superannuation - *Resolving Superannuation Complaints* - options for dispute resolution following the Federal Court decision in *Wilkinson v CARE* (July 1998)

Reports and papers of the Select Committee on Superannuation and Financial Services - 39th Parliament (1999 - 2002)

- *Choice of Superannuation Funds (Consumer Protection) Bill 1999* (November 1999)

- *Superannuation Legislation Amendment Bill (No. 4) 1999* (November 1999)

- *Roundtable on Choice of Superannuation Funds* (March 2000)

- *Provisions of the Superannuation (Entitlements of Same Sex Couples) Bill 2000* (April 2000)

- *New Business Tax System (Miscellaneous) Bill No 2 2000* (June 2000)
- *Financial Sector Legislation Amendment Bill (No 1) 2000* (August 2000)
- *Interim report on the Family Law Legislation Amendment (Superannuation) Bill 2000* (November 2000)
- *Taxation Laws Amendment (Superannuation Contributions) Bill 2000* (December 2000)
- *Family Law Legislation Amendment (Superannuation) Bill 2000* (March 2001)
- *The opportunities and constraints for Australia to become a centre for the provision of global financial services* (March 2001)
- *A 'reasonable and secure' retirement? The benefit design of Commonwealth public sector and defence force unfunded superannuation funds and schemes* (April 2001)
- *Enforcement of the Superannuation Guarantee Charge* (April 2001)
- *Issues arising from the Committee's report on the Taxation Laws Amendment (Superannuation Contributions) Bill 2000* (May 2001)
- *Report on the Provisions of the Parliamentary (Choice of Superannuation) Bill 2001* (August 2001)
- *Prudential supervision and consumer protection for superannuation, banking and financial services - First Report* (August 2001)
- *Prudential supervision and consumer protection for superannuation, banking and financial services - Second Report - Some case studies* (August 2001)
- *Prudential supervision and consumer protection for superannuation, banking and financial services - Third Report - Auditing of Superannuation Funds* (September 2001)
- *Early Access to Super – A Discussion Paper* (November 2001)
- *Early Access to Superannuation Benefits* (January 2002)
- *Investing Superannuation Funds in Rural and Regional Australia - An Issues Paper* (February 2002)

Reports of the Select Committee on Superannuation - 40th Parliament (2002-2003)

- *Taxation Laws Amendment (Superannuation) Bill (No. 2) 2002, and Superannuation Guarantee Charge Amendment Bill 2002* (June 2002)
- *Taxation Treatment of Overseas Superannuation Transfers* (July 2002)
- *Provisions of the Superannuation (Government Co-contribution for Low Income Earners) Bill 2002 and Provisions of the Superannuation Legislation Amendment Bill 2002* (September 2002)
- *Provisions of the Superannuation Legislation Amendment (Choice of Superannuation Funds) Bill 2002* (November 2002)
- *Superannuation and standards of living in retirement – Report on the adequacy of the tax arrangements for superannuation and related policy* (December 2002)
- *Provisions of the Superannuation Industry (Supervision) Amendment Bill 2002 and the Superannuation (Financial Assistance Funding) Levy Amendment Bill 2002* (March 2003)
- *Planning for retirement* (July 2003)

Appendix Five

Current Levels of Portability

Retail superannuation

There are few, if any, limitations on the ability of individuals to transfer balances out of superannuation funds offered by IFSA member companies. Full portability of superannuation is already available to retail investors.

- Retail (personal) superannuation funds do not restrict the circumstances in which consumers can transfer their personal superannuation out of a fund. Consumers can request part or full balance rollovers.
- The majority of corporate superannuation plans in retail (employer) master trust arrangements do not restrict the circumstances in which consumers can transfer funds. Part balance rollovers are widely available from these master trusts although minimum balances may be required to prevent triggering member protection.
- Some corporate superannuation plans in retail (employer) master trust arrangements may require a SIS trigger event (usually leaving the employer) before transferring benefits:
  - In some cases, employers prefer that a SIS trigger event occur before transfer;
  - In some cases, the SIS trigger event rule is part of the master trust's offering to employers; and
  - In either case, the employer may be offering employees choice of superannuation fund, and those employees who prefer another fund, or a fund with no transfer limitations, would not be in this master trust.

Retail (personal) superannuation funds and retail (employer) master trusts do apply various business rules to remaining balances after a rollover:

- Personal superannuation accounts are offered subject to minimum balance requirements as disclosed in offer documents. Remaining balances below these minima may be closed; and
- Corporate superannuation plans in retail (employer) master trusts may have varied business rules on minimum account balances.

Where an account is to be closed after transfer because the account would be below a minimum balance requirement, retail funds have indicated they would prefer to send

the remaining amount to the chosen destination fund, rather than to an eligible rollover fund.

Other superannuation funds

IFSA understands that some, perhaps many, corporate superannuation funds (funds offered by employers, as opposed to master trusts) require a SIS trigger event before transfer. This would usually be leaving the employer by resignation, retirement or retrenchment.

IFSA understands that some multi-employer funds also require a SIS trigger event before transfer, and that some further restrictions may apply as well – such as those intended to retain an account unless the member has left the industry in which the fund operates. We understand that these requirements have decreased in recent years, particularly among the multi-sector, multi-employer funds.

Defined benefit funds generally do not allow portability of superannuation benefits, for reasons that are widely accepted. Unfunded defined benefit superannuation schemes routinely restrict portability of benefits, even after a member has left employment. In many cases, the design of the fund or scheme is such that a transfer amount could not be calculated – for instance, where an employee has not left employment. However, many members of defined benefit funds could be readily provided with a transfer value, and some members of hybrid schemes already have an accumulation-style balance amount yet cannot transfer that balance.

Appendix Six

The Gazetted Portability Regulations

Superannuation Industry (Supervision) Amendment Regulations 2003 (No. 4)[1]

Statutory Rules 2003 No. 196[2]

I, GUY STEPHEN MONTAGUE GREEN, Administrator of the Commonwealth of Australia, acting with the advice of the Federal Executive Council, make the following Regulations under the *Superannuation Industry (Supervision) Act 1993*.

Dated 30 July 2003

G. S. M. GREEN
Administrator

By His Excellency's Command

HELEN COONAN
Minister for Revenue and Assistant Treasurer

1 Name of Regulations

These Regulations are the *Superannuation Industry (Supervision) Amendment Regulations 2003 (No. 4)*.

2 Commencement

These Regulations commence on 1 July 2004.

3 Amendment of *Superannuation Industry (Supervision) Regulations 1994*

Schedule 1 amends the *Superannuation Industry (Supervision) Regulations 1994*.

Schedule 1 Amendments

(regulation 3)

[1] Subregulation 1.03 (1), definition of *protected member*

substitute

protected member has the meaning given by regulation 1.03B.

[2] Subregulation 1.03 (1), after definition of *transferable benefits*

insert

unfunded public sector superannuation scheme means a regulated superannuation fund that is declared to be an unfunded defined benefits superannuation scheme under regulation 2A of the *Superannuation Contributions Tax (Assessment and Collection) Regulations 1997*.

[3] Subregulation 1.03 (3)

omit

[4] Subregulation 1.03AA (3)

omit

[5] After regulation 1.03AB

insert

1.03B Meaning of *protected member*

(1) A ***protected member*** is a member of a regulated superannuation fund who has a withdrawal benefit, or a benefit of any other type that is payable on leaving the fund otherwise than voluntarily (not including any applicable exit fee), that:

(a) is less than $1 000; and

(b) contains, or contained, benefits that are mandated employer-financed benefits (within the meaning of subregulation 5.01 (1)).

(2) An excluded member is not a protected member.

(3) If the trustee of a regulated superannuation fund has rolled over or transferred an amount that is the whole or part of a member's withdrawal benefit to another regulated superannuation fund or to an approved deposit fund, RSA or EPSSS in accordance with Division 6.5, the member is not a protected member of the fund from which the amount was rolled over or transferred.

(4) For subregulation (1), a benefit in a fund is taken to contain or to have contained mandated employer-financed benefits unless:

(a) if the benefits arose in relation to contributions made before 1 July 1995 — the trustee of the fund reasonably believes otherwise; or

(b) if the benefits arose in relation to contributions made on or after 1 July 1995 — the trustee of the fund knows otherwise.

[6] Subparagraph 6.17 (2) (a) (ii)

omit

Division 6.4

insert

Division 6.4 or 6.5

[7] Subregulation 6.20A (6), except the note

omit

[8] Subregulation 6.20B (5), except the note

omit

[9] Division 6.4, heading

substitute

Division 6.4 General rules for rollover and transfer of benefits in regulated superannuation funds and approved deposit funds

[10] Division 6.5

substitute

Division 6.5 Compulsory rollover and transfer of superannuation benefits in regulated superannuation funds and approved deposit funds

6.30 Application

(1) This Division applies:

(a) to a regulated superannuation fund, other than a fund mentioned in paragraph (2) (a) or (b); and

(b) to an approved deposit fund.

(2) This Division does not apply:

(a) to an unfunded public sector superannuation scheme; and

(b) to a self-managed superannuation fund; and

(c) in respect of a defined benefit component of a superannuation interest in a defined benefit fund, if the member who holds the interest is an employee of an employer-sponsor of the fund; and

(d) to benefits that are being paid as a pension (other than an allocated pension).

6.31 Definitions for Division 6.5

(1) Subject to subregulation (2), a ***defined benefit component*** of a superannuation interest is a component of the interest in which the benefits are defined by reference to 1 or more of the following:

(a) the amount of:

(i) the member's salary at the date of the termination of the member's employment, the date of the member's retirement, or another date; or

(ii) the member's salary averaged over a period; or

(iii) salary, or allowance in the nature of salary, payable to another person (for example, a judicial officer, a member of the Commonwealth or a State Parliament, a member of the Legislative Assembly of a Territory);

(b) a specified amount;

(c) specified conversion factors.

(2) A component of a superannuation interest is not a defined benefit component if the only benefits defined by reference to any of the amounts or factors mentioned in subregulation (1) are benefits payable on death or disability.

6.32 Operating standards

(1) For subsection 31 (1) of the Act, a requirement set out in this Division is a standard applicable to the operation of regulated superannuation funds.

(2) For subsection 32 (1) of the Act, a requirement set out in this Division is a standard applicable to the operation of approved deposit funds.

6.33 Request for rollover or transfer of withdrawal benefit

(1) A member of a regulated superannuation fund or an approved deposit fund may, in writing, ask the trustee of the fund to roll over or transfer an amount that is the whole or part of the member's withdrawal benefit.

(2) If the trustee of a fund requires further information in relation to the request, the trustee must, as soon as practicable after receiving the request, ask the member for the information.

6.34 Rollover or transfer of withdrawal benefit

(1) Subject to regulations 6.35 and 6.38, if a trustee of a regulated superannuation fund or an approved deposit fund receives a request under regulation 6.33, the trustee must roll over or transfer the amount in accordance with the request.

(2) Before a trustee of a regulated superannuation fund or an approved deposit fund rolls over or transfers the amount, the trustee must be satisfied that the member:

(a) is aware that the member may ask the trustee for information that the member reasonably requires for the purpose of understanding any benefit entitlements that the member may have, including:

(i) information about any fees or charges that may apply to the proposed rollover or transfer; and

(ii) information about the effect of the proposed rollover or transfer on any benefit entitlements the member may have; and

(b) does not require such information.

Note Under section 1017C of the *Corporations Act 2001*, a trustee of a fund must, on request by a member of the fund, give the member the information and documents mentioned in subsections 1017C (3) and (5). See also regulations 7.9.02, 7.9.45, 7.9.46 and 7.9.83 of the *Corporations Regulations 2001*.

(3) The trustee must roll over or transfer the amount as soon as practicable, and in any case within 90 days, after:

(a) receiving the request; or

(b) if the trustee required further information in relation to the request — receiving the further information; or

(c) if there is a suspension under regulation 6.36 or 6.37 — the end of the period of the suspension.

6.35 When a trustee may refuse to roll over or transfer an amount

(1) A trustee may refuse to roll over or transfer an amount under regulation 6.34 if:

(a) the fund or RSA to which the member has requested the amount be rolled over or transferred will not accept the amount; or

(b) the amount to be rolled over or transferred is part only of the member's interest in the fund, and the effect of rolling over or transferring the amount would be that the member's interest in the fund from which the amount is to be rolled over or transferred would be less than $5 000; or

(c) the trustee has, under regulation 6.34, rolled over or transferred an amount of the member's interest within 12 months before the request is received.

(2) If a trustee refuses to roll over or transfer an amount under subregulation (1), the trustee must tell the member of the refusal in writing.

6.36 Suspension or variation of obligation to roll over or transfer amounts by APRA

(1) This regulation applies if APRA believes, on reasonable grounds, that a rollover or transfer of an amount by the trustee of a regulated superannuation fund or approved deposit fund under regulation 6.34 would have a significant adverse effect on:

(a) the financial position of the fund; or

(b) the interests of other members of the fund.

(2) APRA may, by notice in writing to the trustee, suspend or vary an obligation of the trustee under regulation 6.34.

(3) A suspension or variation under subregulation (2) applies for the period specified by APRA in the notice.

6.37 Suspension or variation of obligation to roll over or transfer amounts by APRA — application by trustee

(1) This regulation applies if the trustee of a regulated superannuation fund or approved deposit fund applies to APRA for a suspension or variation of the trustee's obligation to roll over or transfer amounts under regulation 6.34.

(2) The application must contain information about the fund's financial position and the effect of any rollovers or transfers of amounts under regulation 6.34 on:

(a) the financial position of the fund; or

(b) the interests of other members of the fund.

(3) APRA may ask the trustee to provide further information in relation to the application within the period specified by APRA.

(4) If the trustee does not provide the further information within the specified period, APRA may treat the application as if it had been withdrawn by the trustee.

(5) APRA must consider the application and notify the trustee of its decision in writing, within 30 days after the later of:

(a) the day APRA receives the application; and

(b) the day APRA receives the further information.

(6) If APRA believes, on reasonable grounds, that a rollover or transfer of an amount under regulation 6.34 would have a significant adverse effect on:

(a) the financial position of the fund; or

(b) the interests of other members of the fund;

APRA may, by notice in writing to the trustee, suspend or vary an obligation of the trustee under regulation 6.34.

(7) A suspension or variation under subregulation (6) applies for the period specified by APRA in the notice.

6.38 Trustee's obligations if APRA suspends or varies obligation to roll over or transfer amounts

(1) If, under regulation 6.36 or 6.37, APRA suspends a trustee's obligation to roll over or transfer amounts under regulation 6.34, the trustee must not roll over or transfer an amount under regulation 6.34 for the period of the suspension.

(2) If, under regulation 6.36 or 6.37, APRA varies a trustee's obligation to roll over or transfer amounts under regulation 6.34, the trustee may roll over or transfer an amount under regulation 6.34 only in accordance with the variation.

Division 6.6 Additional standards for eligible rollover funds

6.39 Obligations of trustees

The trustee of an eligible rollover fund must comply, as soon as practicable, with a request by a member:

(a) to pay a benefit of the member in the fund; or

(b) to pay a benefit in the form of a lump sum.

Notes

1. These Regulations amend Statutory Rules 1994 No. 57, as amended by 1994 Nos. 189 and 432; 1995 Nos. 47, 64, 142, 158, 159, 240, 293, 384 and 430; 1996 Nos. 44, 57, 122 and 344; 1997 Nos. 69, 117, 152, 153, 221, 243, 293, 309, 343 and 415; 1998 Nos. 76, 83, 108, 175, 177, 193, 240 and 312; 1999 Nos. 14, 31, 115, 239, 317 and 356; 2000 Nos. 119, 151, 185, 280 and 281; 2001 Nos. 37, 352 and 353; 2002 Nos. 21, 91, 150, 171, 200 and 353; 2003 Nos. 42, 170 and 171.
2. Notified in the *Commonwealth of Australia Gazette* on 31 July 2003.

Retirement Savings Accounts Amendment Regulations 2003 (No. 2)[1]

Statutory Rules 2003 No. 195[2]

I, GUY STEPHEN MONTAGUE GREEN, Administrator of the Commonwealth of Australia, acting with the advice of the Federal Executive Council, make the following Regulations under the *Retirement Savings Accounts Act 1997*.

Dated 30 July 2003

G. S. M. GREEN
Administrator

By His Excellency's Command

HELEN COONAN
Minister for Revenue and Assistant Treasurer

1 Name of Regulations

These Regulations are the *Retirement Savings Accounts Amendment Regulations 2003 (No. 2)*.

2 Commencement

These Regulations commence on 1 July 2004.

3 Amendment of *Retirement Savings Accounts Regulations 1997*

Schedule 1 amends the *Retirement Savings Accounts Regulations 1997*.

Schedule 1 Amendments

(regulation 3)

[1] Subregulation 1.03 (1), definition of *protected RSA holder*

substitute

protected RSA holder has the meaning given by regulation 1.03A.

[2] Subregulation 1.03 (2)

omit

[3] After regulation 1.03

insert

1.03A Meaning of *protected RSA holder*

(1) A ***protected RSA holder*** is an RSA holder who has a withdrawal benefit, or benefits of any other type that are payable on closing the RSA otherwise than voluntarily, net of any applicable exit fee, that:

(a) are less than $1 000; and

(b) contain, or have contained, benefits that are mandated employer-financed benefits.

(2) If an RSA provider has transferred an amount that is the whole or part of an RSA holder's withdrawal benefit in accordance with section 50 of the Act, the RSA holder is not a protected RSA holder for the RSA from which the amount was transferred.

(3) For subregulation (1), a benefit in an RSA is taken to contain or to have contained mandated employer-financed benefits unless the RSA provider knows otherwise.

[4] Subparagraph 4.20 (1) (a) (ii)

substitute

(ii) being rolled over or transferred under section 50 of the Act or Division 4.4 or Part 4A; and

[5] Paragraphs 4.20 (1) (b) and (c)

omit

under this Part or Part 4A

insert

under section 50 of the Act or this Part or Part 4A

[6] After Division 4.4

insert

Division 4.5 Duty to transfer balance of RSA

4.35 Amount to be transferred (Act s 50)

(1) For subsection 50 (3) of the Act, the amount of the RSA to be transferred is the amount of the RSA holder's withdrawal benefit specified by the RSA holder in the request.

(2) The amount specified by the RSA holder may be the whole, or part, of the RSA holder's withdrawal benefit.

4.36 Operating standard

(1) For subsection 38 (1) of the Act, the standard set out in subregulation (2) is applicable to the operation of RSAs.

(2) Before an RSA provider transfers an amount mentioned in regulation 4.35, the RSA provider must be satisfied that the RSA holder:

(a) is aware that the RSA holder may ask the trustee for information that the RSA holder reasonably requires for the purpose of understanding any benefit entitlements that the RSA holder may have, including:

(i) information about any fees or charges that may apply to the proposed transfer; and

(ii) information about the effect of the proposed transfer on any benefit entitlements the RSA holder may have; and

(b) does not require such information.

Note Under section 1017C of the *Corporations Act 2001*, an RSA provider must, on request by an RSA holder, give the RSA holder the information and documents mentioned in subsections 1017C (3) and (5). See also regulations 7.9.02, 7.9.45, 7.9.46 and 7.9.83 of the *Corporations Regulations 2001*.

[7] Regulation 6.15

omit

Notes

1. These Regulations amend Statutory Rules 1997 No. 116, as amended by 1997 Nos. 150, 151, 242, 294, 308 and 342; 1998 Nos. 82, 176, 178 and 192; 1999 Nos. 13 and 315; 2000 No. 279; 2002 Nos. 20, 47, 90, 149, 200 and 352; 2003 No. 41.
2. Notified in the *Commonwealth of Australia Gazette* on 31 July 2003.

Appendix Seven

IFF's Tabled Document

OtherFunc	TypeOf Policy	ExitFee	AccountBalance	%
Tower	Blue Ribbon Superannuation	$ 8,211.53	$11,223.08	73.17
Tower	Blue Ribbon Super	$ 792.80	$1,299.18	61.02
Tower	Superannuation	$ 4,042.42	$7,699.85	52.50
Tower	Blue Ribbon Executive Supperannuation	$ 959.69	$2,011.71	47.71
Tower	Superannuation	$ 1,505.16	$3,163.93	47.57
Tower	Superannuation	$ 1,579.57	$3,368.81	46.89
Tower	Personal Superannuation	$ 4,462.91	$10,189.54	43.80
Tower	Blue Ribbon Supperannuation	$ 4,492.20	$11,422.27	39.33
Tower	Personal Superannuation Plan	$ 2,825.68	$7,872.71	35.89
Tower	Superannuation	$ 14,893.49	$56,710.48	26.26
Tower	Personal Superannuation Plan	$ 10,130.32	$44,008.14	23.02
Tower	Personal Superannuation Plan	$ 5,698.42	$24,936.09	22.85
Tower	Pesonal Superannuation Plan	$ 2,143.83	$9,604.87	22.32
Tower	Personal Superannuation	$ 2,759.78	$12,877.24	21.43
Tower	Personal Superannuation	$ 4,772.91	$22,319.38	21.38
Tower	Personal Superannuation	$ 2,498.20	$11,924.50	20.95
Tower	Personal Superannuation	$ 9,510.03	$47,010.97	20.23
Tower	Superannuation	$ 40,595.40	$216,705.36	18.73
Norwich	Personal Superannuation	$ 4,044.55	$10,222.66	39.56
Norwich	Superannuation	$ 3,432.49	$11,857.16	28.95
Norwich	Personal Superannuation	$ 2,167.75	$16,669.14	13.00
National M	Personal Super	$ 2,826.69	$16,187.93	17.46
MLC	MasterKey Superannuation (Gold Star)	$ 5,621.11	$5,939.14	94.65
MLC	Superannuation	$ 3,155.52	$6,904.50	45.70
MLC	Superannuation	$ 6,374.64	$22,380.17	28.48
MLC	MasterKey Superannuation (Gold Star)	$ 6,090.67	$21,694.00	28.08
MLC	MasterKey Superannuation (Gold Star)	$ 830.11	$3,846.96	21.58
MLC	MasterKey (Gold Star) Superannuation	$ 3,219.36	$16,240.22	19.82
Macquarie	ADF Superannuation Fund	$ 12,958.93	$68,707.10	18.86
ING	Personal Retirement Plan	$ 2,178.79	$15,689.69	13.89
ING	Plus Policy	$ 3,463.85	$27,899.28	12.42
ING	Master Fund	$ 3,538.79	$28,843.34	12.27
ING	Personal Retirement Plan	$ 1,077.00	$8,890.00	12.11
ING	Personal Retirement Plan	$ 3,422.18	$29,793.84	11.49
Colonial	Umbrella Financial Plan Superannuation	$ 2,502.39	$7,793.28	32.11
AXA	Retirement Security Plan	$ 1,195.27	$1,287.80	92.81
AXA	Retirement Security Plan	$ 1,258.87	$1,371.21	91.81
AXA	Retirement Security Plan	$ 2,361.77	$3,900.41	60.55
AXA	Superannuation	$ 3,615.26	$5,985.52	60.40
AXA	Superannuation	$ 2,248.18	$3,870.01	58.09
AXA	Retirement Security Plan	$ 5,653.37	$10,486.06	53.91
AXA	Personal Superannuation	$ 4,270.27	$8,063.69	52.96
AXA	Retirement Security Plan	$ 4,227.00	$8,230.37	51.36
AXA	Retirement Security	$ 1,445.10	$2,976.12	48.56
AXA	Superannuation	$ 5,414.39	$12,303.80	44.01
AXA	Retirement Security Plan	$ 1,125.32	$2,587.62	43.49
AXA	Retirement Security Plan	$ 4,151.06	$9,983.54	41.58
AXA	Reitirement Security Plan	$ 1,088.50	$2,721.24	40.00
AXA	Superannuation	$ 5,793.37	$15,852.77	36.54
AXA	Retirement Security Plan	$ 1,038.23	$3,229.75	32.15
AXA	Retirement Security Plan	$ 2,979.26	$9,358.76	31.83
AXA	Retirement Security Plan	$ 2,029.96	$7,905.96	25.68
AXA	Superannuation	$ 5,236.61	$21,021.37	24.91
AXA	Superannuation	$ 4,071.44	$16,862.97	24.14
AXA	Personal Superannuation	$ 3,460.25	$16,893.74	20.48

AXA	Retirement Security Plan	$ 7,406.90	$36,256.60	20.43
AXA	Retirement Security Plan	$ 4,207.13	$20,946.65	20.08
AXA	Personal Superannuation	$ 5,311.05	$26,540.42	20.01
AXA	Retirement Security Plan	$ 6,306.62	$32,202.82	19.58
AXA	Retirement Security Plan	$ 8,056.36	$42,406.40	19.00
AXA	Superannuation	$ 1,719.56	$9,367.63	18.36
AXA	Employer Sonsored Superannuation	$ 4,022.00	$22,334.89	18.01
AXA	Retirement Security Plan	$ 9,325.35	$52,478.14	17.77
AXA	Retirement Security Plan	$ 1,200.91	$7,190.48	16.70
AXA	Personal Superannuation	$ 1,436.54	$8,684.01	16.54
AXA	Managed Fund	$ 1,829.86	$11,978.86	15.28
AXA	Retirement Security Plan	$ 2,051.45	$13,662.75	15.01
AXA	Retirement Security Plan	$ 1,326.84	$9,172.38	14.47
AXA	Superannuation	$ 1,922.55	$13,944.72	13.79
AXA	Retirement Security Plan	$ 5,043.29	$38,702.53	13.03
AXA	Superannuation	$ 1,331.76	$11,322.06	11.76
AXA	Superannuation	$ 2,157.31	$18,909.02	11.41
AXA	Retirement Security Plan	$ 4,929.99	$43,530.66	11.33
AXA	Retirement Security Plan	$ 2,179.29	$19,983.43	10.91
AXA	Retirement Security Plan	$ 2,463.59	$23,421.85	10.52
AXA	Superannuation	$ 2,057.76	$20,208.59	10.18
AXA	Superannuation	$ 1,002.84	$10,128.90	9.90
AXA	Retirement Security Plan	$ 6,219.94	$63,184.32	9.84
AXA	Retirement Security Plan	$ 2,301.75	$24,966.90	9.22
AXA	Personal Superannuation	$ 3,573.12	$39,099.40	9.14
AMP	Endowment	$ 5,240.65	$8,391.93	62.45
AMP	Investment Linked Regular Premium Plan	$ 2,146.37	$5,352.45	40.10
AMP	Investment Linked Super	$ 1,593.34	$7,685.03	20.73

Appendix Eight

IFSA's Supplementary Submission

Investment & Financial Services Association Ltd
ACN 080 744 163

12 August 2003

The Secretary
Senate Select Committee on
Superannuation and Financial Services
Parliament House
CANBERRA ACT 2600

Dear Mr Frappell

Reference:

Portability of Superannuation – Response to Document Tabled 1 August

The Investment and Financial Services Association would like to provide the Committee with comments in response to the document tabled at the Melbourne public hearing on 1 August 2003.

The document listed a number of claimed 'exit fees' from retail superannuation funds offered by IFSA member companies. The witness stated that these were actual cases obtained from an organisation known as Industry Funds Financial Practice. IFSA has consulted with the companies named.

There are two very significant errors of fact in the witness' claims.

- The document claims exit fees were levied by at least one fund that does not charge any exit fee, and which has never charged any exit fee.

- The witness asserted "many of the instances I have spoken of … are from modern day master trusts". This claim is not true, so far as we can ascertain from the limited product descriptions in the document.

One fund offered by an IFSA member company is listed in the document as charging an exit fee, although the fund named has never charged and exit fee and does not charge entry fees. The company (Company E) has categorically confirmed that no such fee has ever been charged.

IFSA can find no example in the tabled list of an exit fee levied in master trust open to new members, as the witness appears to have asserted. Critically, the implication that investors who join master trusts now could be levied exit fees of the levels listed in the document is false. There are closed, old-style products where the member has 'traded up' to a master trust environment while retaining the existing contract conditions. IFSA is advised that no new member of a master trust, even where the

Level 24, 44 Market Street, Sydney NSW 2000 Ph: 61 2 9299 3022
Email: ifsa@ifsa.com.au Fax: 61 2 9299 3198

master trust now encompasses these traded-up policies, can face an exit fee such as those claimed in the tabled document.

The witness gave an example of a master trust where holders of old-style products have been included in part of the ongoing master trust through a trade-up process. The original product is no longer sold and no new member joining the master trust would be covered by those fee structures. If this example is the basis of the witness' claim that 'modern day master trusts' have high exit fees, it is incorrect.

In the case of the fund that has never charged exit fees, the amount claimed as an exit fee appears to be a tax amount. If tax is confused with exit fees in this case, we are concerned that other claimed exit fees could include tax.

Given two significant errors of fact, and a possible confusion of exit fees for tax, IFSA is very concerned that the Committee not draw conclusions from this evidence.

The document provides very little detail of the circumstances of the alleged fees and the witness asserted that the amounts listed as 'exit fees' were, or would have been, levied on the stated account balances on exit. The witness described them as 'excessive fees and penalties', and asserted that these were 'mainly comprised of employer contributions mandated by federal parliament'. It appears that both these comments were made in respect of the examples tabled; yet there is simply insufficient detail in the list to determine the basis of the alleged fees and whether in fact they do include mandated employer contributions.

IFSA has not claimed, and is not claiming here, that there may not be circumstances in which significant 'exit fees' can arise. In our original submission, we set out four types of fees that may be referred to as exit fees, including two types of fees in closed products.

- Early termination fees in closed products. These fees were set in superannuation products offered through life insurance offices, and recovered up front costs incurred by the life office. They are often calculated on the first year's premium and reduce over a set period of, say, five years. The proportionate impact of these fees also reduces the longer a product is held because the first year's premium becomes a smaller and smaller proportion of the balance.
- Early termination of contract (traditional policies – whole of life, endowment or pure endowment). Traditional policies were structured on a long-term basis usually comprising an investment and, in earlier years, an insurance component. The contracts operated on the basis of a guaranteed maturity value at a date in the future. Up front costs were incurred meaning that in the first few years of operation, the surrender/cash value of the policy was nil, or significantly less that what had been paid in. Defaulting on the contractual terms would create a significant gap between what would have been paid, both as a guarantee and in bonuses, had the contract run to maturity. Provided that clients have met the conditions of the contract, most traditional super policies have probably been in force for so long that this position no longer applies. These contracts were formulated in a very different environment and, given their long-term structure, do not suit early withdrawal or partial cashing

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(although bonuses may generally be taken early). These contracts are no longer offered.

I have attached comments made by five of the companies named in the tabled list. For commercial confidentiality, these remarks do not identify particular companies or products.

It is unfortunate that the committee has made a decision to release the material without first verifying all of the facts. There has already been newspaper reportage quoting extracts from the document. The document tabled contains errors of fact, which if published, could cause commercial damage.

Yours sincerely

Richard Gilbert
Chief Executive Officer

Level 24, 44 Market Street, Sydney NSW 2000 Ph: 61 2 9299 3022
Email: ifsa@ifsa.com.au Fax: 61 2 9299 3198

Comment on Tabled Document: Company A

The names on the list are not all product names but generic descriptions. The company cannot identify the specific products from these descriptions.

All products of this type have been closed for new member sale.

The products were designed as long term investments to be held to long term retirement. The exit fee is only paid if the contract is broken early.

Each contract had a target duration from the outset. This was the date by which the exit fee would reduce to zero

As these are longer term investments the design was to spread the costs over a longer period

The general structure of the termination fees was that they reduced as contributions were paid and the savings built over the life of the superannuation policy.

An exit fee might arise if the member broke the contract early and the earlier that happened in the contract term the larger the fee would tend to be.

Where a person stopped paying contributions the exit fee would no longer reduce as quickly as planned.

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Comment on Tabled Document: Company B

Without further information the company cannot investigate the specific circumstances surrounding the examples outlined, however, it appears that the accounts referred to are older style superannuation policies. This kind of superannuation savings policy was standard in the 1980's and early 1990's across the financial services market.

During this time, superannuation policies were designed as long-term savings policies where the investor's funds were committed to a single provider until retirement. This involved a mutually agreed long-term contract and reflected superannuation industry practice at the time. Generally, these policies remain viable retirement savings vehicles for investors who continue to contribute to these accounts for the duration of the contract.

The company can confirm that it has not issued accounts of this nature since the mid 1990's. The company supports the transparent disclosure of fees to investors and allowing investors to move their funds at any time.

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Comment on Tabled Document: Company C

The list of products presented to the Committee included a product issued by a former life office during the period commencing in the late-1980s up to the close of the product in May 1999. The illustration shows that the exit fee amounted to 32% of the account balance. The information provided by the Committee was insufficient to verify the accuracy of the exit fee ratio. The structure of the product allowed for a variety of distribution conditions and some included high distribution/advising costs recouped through high exit fees on surrender at short durations.

Exit Fees versus Entry Fees

The product design offered exit fees as a replacement for entry fees. Generally, all savings based products carried fees to cover the cost of distribution. Products with exit fees did not carry any particular bias in pricing compared to products structured with entry fees. Some policyholders who had early surrenders on the entry fees products would have paid similar distribution costs to the case illustrated in the Committee's evidence.

Upfront Expenses on Long-Term Products

During the decades of 1980-90, personal superannuation products were sold as long-term savings vehicles. When the up-front high distribution costs were spread over the contractual term, the expense loading appeared reasonable (in terms of the values of the day). The unreasonable nature of the charge was crystallised when the policyholder exercised options to surrender the policy before the contractual period had been completed. There are policyholders who will continue to pay the premiums on their policies and who will be satisfied with the distribution charges collected over the full contractual term.

Product Disclosure Standards

The industry and regulator participated in developing compliance requirements for disclosure of fees and charges in the 1980-90s. The foundation for disclosure requirements now enforced through FSRA was laid during this period. During that period the product brochures kept pace the rapidly evolving disclosure requirements. the adjustments to reflect collectible unamortised exit fees.

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Comment on Tabled Document: Company D

Product pricing structure

This product is a regular premium personal superannuation product that was developed in the 1970s as a long-term savings plan to provide financial security for members in retirement. The fee structure is not unique, it is similar to the fee structures of products offered by other financial services companies at the time it was developed and sold.

The product was designed to reward members who commence their contributions at an early age and continue these through to their Selected Retirement Date (SRD). If the member stays in the plan until their SRD, no exit penalties are charged and the member benefits from a fee structure that declines as the savings accumulate. The ongoing fees and charges for a contributing member are generally a lot lower than many other products currently on the market, over the life of the policy.

Contributions are paid into the client's account. The Basic Account receives the first two years of contributions (and the first two years of any increase in contributions), while the Investment Account receives all contributions made in the third and subsequent years as well as any single, one-off contributions or additions.

The charging structure is such that the upfront expenses incurred in establishing a contract are not deducted as a one-off establishment charge. Rather, they are deducted using the Basic Account management charge over the term of the contract to the SRD.

As stated previously, members are rewarded through lower management charges as savings accumulate. The account management charges are as follows:

Table 1

	Basic Account Charge	Investment Account Charge
Total Account balance < $20,000	3% pa	0.5% pa
Total Account balance $20,001 - $40,000	2.75% pa	0.375% pa
Total Account balance $40,001 +	2.5% pa	0.25% pa

In addition to the account management charge (basic account charge and investment account charge), an asset management fee is deducted before our unit prices are set on the underlying portfolios. This asset fee is 1.15% pa for the Guaranteed and Managed portfolios, 1.20% pa for the Growth portfolio and 1.25% pa for the High Growth portfolio. An additional charge of 0.6% pa applies on the Guaranteed portfolio to cover the costs associated with providing the capital guarantee.

For ongoing contributions (ie after the first two years), the maximum charge (including the account management charge and asset management charge) for members in the Managed portfolio (the majority of members) is 1.65% pa. This reduces to 1.40% pa for members with an account balance that exceeds $40,000:

Exit Fee

The charging structure is designed so that the fees are distributed over the expected life of the plan, rather than as a high establishment cost. The exit fee is in place to recover the initial costs associated with commencing the plan as a lump sum should the length of the contract be reduced. The fee is calculated as follows:

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The balance of the Basic Account is discounted by a given factor for each year remaining to the Selected Retirement Date (or part thereof). The factor applied is relative to the size of the Basic Account Balance as follows:

Table 2

Basic Account Balance	Exit Fee
<$10,000	4% x Basic Account Balance x Years to SRD
$10,001 - $20,000	3.5% x Basic Account Balance x Years to SRD
$20,001 +	3% x Basic Account Balance x Years to SRD

This product was designed 20 years ago in a way that was consistent with the products offered by other retail superannuation providers at that time with the aim of encouraging people to save for their retirement. However, customer requirements have changed over time, and the market now demands more flexibility. Products on sale now are designed and priced to offer flexibility in the early years, rather than being focused purely on the value at retirement.

Recent Improvements

In recognising this trend, the company has implemented a number of changes to modernise the contract and review the investment options available under the contract, in an effort to improve our members' benefits.

The company undertook extensive independent market research to produce a package of changes which overall improve member benefits. The charging structure was revised in July 2001 so that all future contributions (including the first two years of any increase in contributions) are allocated to the lower cost Investment Account. This also ensures that any future increase in contributions is not considered in the exit fee calculation (which is a proportion of the Basic Account balance). The company also introduced additional investment portfolios to cater for all risk profiles. These changes were a significant investment for the company and were aimed at improving member benefits and retaining these clients in the product.

Using the market research the company also designed a conversion offer to its on-sale products. This initiative was included in recognition of those clients who are after more extensive investment options than available in the newly improved product. This conversion offer effectively grandfathers 5% of this product's exit fee in the new products.

The company has made significant changes to this product and believes these changes make it a very competitive product in the retail superannuation market. This product will not always be suitable for the needs of all members and in these circumstances alternative products may need to be considered.

The company believes that this product is now a viable investment to be retained by members as part of an overall portfolio of diversified asset classes and products. It is one of the only products in the retail superannuation market that offers a Capital Guaranteed portfolio to members, which can be an attractive option when market returns fall.

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Comment on Tabled Document: Company E

Superannuation fund

The superannuation fund is a nil-entry fee, nil-exit fee fund used widely by investors and advisers. It currently has almost 27,000 members in the fund.

The superannuation fund does not charge entry or exit fees. The fund has been in operation since November 1984, initially as an approved deposit fund which now operates as a superannuation fund under SIS. At no time has the trust deed allowed the trustee to charge an exit fee. The fund can deduct amounts for reimbursement of taxes paid, in addition to annual management and expense recovery fees. All fees and taxes have been clearly disclosed in the offer documents and annual reports for the fund.

Although we do not know the facts of this particular case, we can only assume that what appears more likely to be a taxation liability has been incorrectly characterised as an exit fee.

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Appendix Nine

IFF's Supplementary Submission

INDUSTRY FUND SERVICES

ROLLOVER SERVICE ANALYSIS

Prepared August 2003

By
Melissa Birks
Maxine Douglass

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Appendix A: Rollover Service Recommendation Data

1. Introduction

The purpose of this report is to detail the activity of the IFS Member Services Rollover Service and looked at the recommendations made by the Rollover Service concerning exit penalties charged by other funds when members consider rolling over to another fund.

The report will also look at the time taken by other funds to administer requests for information and ultimately process rollovers.

2. Overview

2.1 Time frames

The time frame chosen for the purposes of this report is July 2001 to 30 June 2003.

2.2 Data Source

The data used is this report has been collected from the Rollover Service database.

The Rollover Service provides analysis and recommendations to industry fund members regarding whether it is in their financial interest to roll money out of their other superannuation funds into their industry account. A recommendation is made based on the fees and charges associated with their other fund compared to their industry fund.

Data is recorded on a specially designed access database it records time frames, fee information and the advice provided. Due to privacy considerations, data identifying specific individuals has not been included, e.g. member names, address, member numbers, etc.

3. Results

3.1 Recommendations

3.1.1 All Recommendations

For the period from 1 July 2001 to 30 June 2003 the Rollover Service produced at total of 2310 recommendations. 40% of all policies analysed had some form of exit penalty attached to them.

Each recommendation was made based on information provided by other funds. This information was then compared with the fee structure of the balanced fund of the member's industry fund. Subject to the fee information provided by the other fund, two basic types of rollover recommendation were made. They were:

1. Rollover Recommendations
    a. No exit penalty
    b. Exit penalty

2. Do Not Rollover Recommendations
    a. Issue other than exit penalty
    b. Exit penalty

For detailed information regarding the recommendations please see Appendix A.

3.1.2 Recommendation to Rollover

Out of the total number of recommendations made, 1923, or 83.2%, were to rollover, of which 1196 had no exit penalty and 727 had an exit penalty.

Recommendation	Number of Policies	% of 'do rollover'	Approx Total Account Balance	Approx. Exit Penalty
Rollover - No exit penalty	1196	62	$26m	n/a
Rollover - Exit penalty	727	38	$19m	$0.63m

3.1.2.1 No exit penalty

The value of rollovers recommended where there was no exit fee was

3.1.2.2 Exit penalty

The 727 recommendations to rollover were despite an exit penalty represent 37.8% of recommendations to rollover, and 31.5% of all recommendations made.

Where a recommendation is made to rollover despite their being an exit penalty, it has been assessed that the exit penalty would be recuperated over time due to the fee savings made by rolling into an industry fund, i.e. the industry fund had lower investment management fees, no contributions fees, no adviser fees etc.

The total value of exit penalties for these recommendations was $626,982, or 34.5% of the value of the corresponding total account balance ($18.2 million)

Where the recommendation was to rollover despite an exit penalty, 137 of the policies were from AXA and 131 were MLC, representing 18.8% and 18% respectively of the total (727).

3.1.3 Do Not Rollover Recommendations

Of the total recommendations made, 387 were recommendations not to rollover. This represents 16.8% of all recommendations.

Do not rollover recommendations can be further broken down into two categories based on the reason not to rollover. The reasons are:

1. Issues other than identifiable exit penalties
2. Exit penalties

3.1.3.1 Issues other than Exit Penalties

193 policies were recommended not to rollover due to issues other than exit penalties, representing approximately 8.4% of all recommendations. The value of these policies was $4,165,729.

There are three main reasons why a rollover is not recommended in this category. They are:

1. Other fund has fees which are lower and there is no exit penalty
2. Other fund has lower fees and there is an exit penalty
3. Other fund is an endowment/whole of life policy

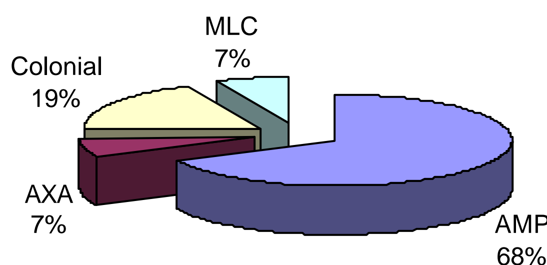
The first case we highlight the benefits of consolidation and recommend the member look at investment returns.

The second case we highlight the benefits of consolidation but recommend that it may be advisable to speak to a financial planner.

Endowment policies are recommended not to rollover due to the forfeiture of terminal and reversionary bonuses. Endowment policies represent 31% of the193 policies in this category. The account value of these endowment policies represent was $1.2m, or 29%, of the total account value ($4.2m) of all policies where recommended not to rollover for issues other than exit fees.

AMP accounted for 68% of all do not roll endowment policy recommendations – see Chart 1 below.

Chart One - Endowment Policies by Fund



3.1.3.2 Exit Penalties

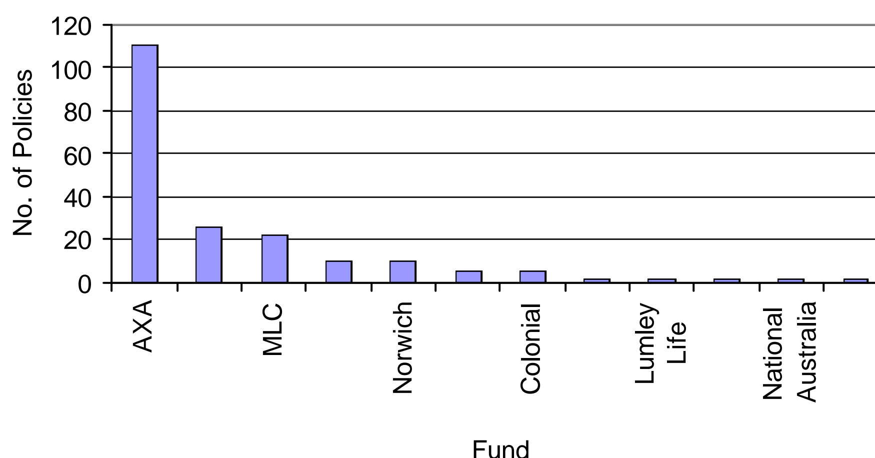
194 policies were recommended to not rollover due to exit penalties during the period 1 July 2002 to 30 June 2003. This figure represents 50% of recommendations to not rollover and 8.4% of all recommendations.

The total value of exit penalties identified was $747,994, that is 19% of the corresponding account balances ($3.9m)

It is interesting to see that in cases were recommendations where made not to rollover due to exit penalties, AXA policies account for 111, or 57%, of the 193 policies where a rollover was not recommended due to exit penalties. See Chart 2 below for the number of policies by all funds in this category. AXA's 111 policies had exit penalties that accounted for 48.7% ($347,668) of the total value of exit penalties identified in this category.

The next highest was Tower with 26 polices, i.e. 13.4% of all policies in this category. Tower's exit penalties account for 20.3% of the total value of exit penalties.

Details of all exit penalties can be found in Appendix A.



Tables 1 & 2 show, by fund, the top three policies by exit fee value and exit fee as a percentage of account balance during 1 July 2001 to 30 June 2003.

Table One –Top three exit penalties by dollar value

Fund	Exit Penalty Value	Exit Penalty as % of Acc Bal
Colonial	$52,482.65	71 %
Tower	$40,595.40	19%
Tower	$14,893.49	26%

Table Two - Top three exit penalties as a proportion of account balance

Fund	Exit Penalty Value	Exit Penalty as % of Acc Bal
MLC	$3,297.69	100.72%*
AMP	$2,031.87	100.00%
MLC	$ 8,050.31	94.98%

* This represents exit penalties plus shortages

Details of all other individual e xit penalties can be found in Appendix A.

3.2 Response Times

There are two specific occasions where the time taken by the other fund to respond to requests can significantly impact on the service provided by the Rollover Service and ultimately the value of the account rolled over.

The two occasions are:

1. the time taken by other fund to respond to fee information requests by the rollover Service and,

2. the response time by the other fund to administer a rollover request.

3.2.1 Fee Information Request

The median response time for information requests across all funds is 17 days. However, Tower is the slowest by taking a median response time of 38 days to provide information.

Table Three - Median and mean number of days taken by funds to respond to fee information requests.

Fund	**Mean** (No. of Days)	**Median** (No. of Days)
All Funds	22.899	17
AMP	22.59	16
AXA	14.773	10
Colonial	26.788	18
ING	35.233	25
MLC	22.714	17
Tower	37.2	38

3.2.2 Rollover Request Completion

The median response time for administering rollover requests for all funds is 15 days. However, Tower again was the slowest with a median turn around time of 32 days, which is 2.1 times longer than the all fund median.

Table Four - Median and mean number of days taken by funds to process rollover requests.

Fund	**Mean** (No. of Days)	**Median** (No. of Days)
All Funds	24.125	15
AMP	20.51	14
AXA	29.271	15
Colonial	25.937	15
ING	18.458	15
MLC	28.566	17
Tower	45.28	32

Delays in responding to rollover requests can have a serious impact on members account balance as market values fluctuate daily. This is particularly true in the present climate where socio economic and political issues adversely impact domestic and international market activity.

4. Conclusion

4.1 Exit Penalties

From the information in this report and Appendix A, it is apparent that negative impact of exit penalties on account values is very real.

Members can make a choice whether to rollover as the exit penalty they are charged can be recuperated over time due to the fees saving made in an industry fund.

However, as the Rollover Service demonstrates, some members have to miss out on lower on going fees as the exit fee is so high it can not be recuperated despite fee savings. Alternatively, members severely disadvantage their account balance where they decide to pay the exit penalty and rollover.

4.2 Response Times

The response times experienced by the Rollover Service from most funds is acceptable. However, for both requests for information and processing rollovers, Tower takes a considerably longer than the average. It has been established that one of the main reasons for the extra time taken by Tower is due to older Tower policies details not being store electronically and information being sourced from archives.

Delays in responding to rollover requests can have a serious impact on members account balance as market values fluctuate daily. This is particularly true in the present climate where socio-economic and political issues adversely impact domestic and international market activity.

Appendix A

See excel file titled 'Rollover Recommendations 2001-03'