Submission to

Senate Select Committee on Superannuation

Inquiry into

Portability of Superannuation

by

The Association of Superannuation Funds of Australia Ltd

July 2003

Inquiry into

PORTABILITY OF SUPERANNUATION BENEFITS

This submission is in response to the Senate Select Committee on Superannuation's inquiry into Portability of Superannuation following the Senate's referral to the Committee of the draft Superannuation Industry (Supervision) Amendment Regulations 2003 and the draft Retirement Savings Account Amendment Regulations 2003.

The Association of Superannuation Funds of Australia (ASFA) has previously provided comments on the draft regulations to the Government and has expressed its concern with the Government's proposed treatment of portability as a 'stand alone' issue. ASFA considers that such an approach has the potential to adversely impact members retirement benefits and that it will not meet the government's primary policy objectives for portability as set out in the consultation paper on portability.

Objectives of the proposal

The Government's Consultation Paper on portability defines *portability of superannuation benefits* as 'the ability of a member to transfer superannuation benefits from one superannuation fund, approved deposit fund (ADF) or Retirement Savings Account (RSA) to another fund, ADF or RSA or exempt public sector superannuation scheme (EPSS)'.

The paper argues that the extension of portability would "assist in addressing the issue of multiple superannuation accounts". This has been taken to reflect Government concern over the large number of accounts reported to the ATO as lost or inactive and a belief that a lack of portability is the main cause.

Although not in the formal objectives, the Minister has also publicly referred to the importance of consumers being able to get out of "poorly performing funds".

State of play

There are currently eight million people with 20 million superannuation accounts. In some cases people have multiple accounts (funds) because they have a number of jobs simultaneously and their employers contribute to different funds on their behalf. This may happen for instance where a person works part time in a public hospital and in a private hospital because public sector funds are generally unable to take on private sector employer-sponsors.

In most cases, however, the multiple accounts are the result of the person's failure to consolidate accounts once they have left one employment situation and commenced another. A lot of the accounts are therefore inactive, i.e. not receiving any current contributions.

The major disadvantage of multiple accounts relates to consumers losing track of their super savings and the additional fees and charges that are required to administer such accounts. But for some consumers the decision to retain more than one account may be a deliberate and informed decision.

Current arrangements for portability

a) A person is able to move their superannuation to another fund once their current employer ceases contributing, i.e. when they leave that particular job.

Exceptions may arise:

- where the employee is a member of an unfunded public sector scheme, or
- where the person has more than one employer contributing to their account in the fund on their behalf. If the person leaves one employer but continues with the other, the portability conditions are not met until that employment ceases.

b) Members of funds who have no employer support (personal or retail superannuation) are able to move their superannuation to another fund at any time.

Impediments to current portability arrangements

The major impediment to current portability arrangements appears to be lack of motivation.

In September – October 2002 a joint industry/ATO campaign heightened community awareness and information as to how to track and reclaim "lost" superannuation accounts. Many funds now offer assistance to new (and continuing) members in moving inactive superannuation accounts to the current fund used by the member. Those funds that participated in this process have found it to be very successful.

In some cases a person may be dissuaded from consolidation by high exit penalties (eg old style life products). But it would be difficult to remove these existing contractual arrangements.

ASFA is of the view that the proposed regulations will not assist the stated aim of the Government's 2002 consultation paper on portability of assisting "in addressing the issue of multiple superannuation accounts. As outlined earlier, the multiple accounts issue arises primarily from account holders not amalgamating accounts where they are currently able to do so. Further the proposed regulations, if not linked directly to choice of fund, could result in a proliferation of additional accounts if members are encouraged to transfer from their current superannuation provider to the 'next best thing' without the ability to also direct future contributions to that same provider.

Strategy going forward

In both the Government's general policy statement *Heading in the right direction – securing Australia's future*[1] and its pre-election statement on superannuation, *A Better Superannuation System*[2], 'portability' was directly associated with 'choice'. The direct linking of the twin policies of portability and choice was confirmed in the 2002 Budget Papers. This submission strongly supports that position.

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.

The proposed regulations, if introduced without choice of fund, would mandate the right of a member to transfer account balances from a fund while the employer continued to contribute to that fund. This would result in an increased number of accounts, churning of transfers (with associated costs, administration and risk of fraud), increased costs to consumers. The remaining small account balances also potentially add to increased costs for the Fund. It is our understanding that although the exiting fund would not be required to "protect" small member accounts the receiving fund still would be required to do so.

Disclosure and education

The importance of informed choice and selection of fund remain critical.

ASFA has stressed continually that for informed choice of fund a robust system of disclosure, which fosters understanding of and comparability between funds, is necessary. An education campaign which increases the population's financial literacy, not just the mechanics of exercising choice, is also needed. **Whether portability and choice are delivered separately or together, these disclosure and education needs will still exist.**

ASFA is cognisant of the fact that some consumers wish to leave a fund that they perceive as not performing well or as badly managed. However, if the government introduced portability without choice, consumers would still need an effective disclosure regime and adequate financial skills to choose another fund which met their requirements. In a portability regime, as in a choice regime, uninformed consumers

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[1] [1] "**SUPERANNUATION THE ROAD AHEAD**

Press ahead with reforms to give Australians choice of superannuation fund and to facilitate portability of members' balances between funds."

[2] "**Choice of Superannuation and Portability**

The Coalition believes that workers should have the freedom to decide who manages their superannuation and the right to move their superannuation benefits from one fund to another"

and

"The Coalition remains committed to choice and portability in superannuation, which will benefit Australian workers by creating greater competition in the superannuation industry, resulting in reduced fees and charges and more responsive investment strategies by trustees."

would also be vulnerable to unscrupulous advisers who sought to increase their own rewards rather than their client's retirement savings.

Portability on its own may also lead to erosion of the preservation rules through the transfer and then cashing out of amounts less than $200.

Fees

ASFA supports the absence of a restriction on exit fees where these fees reflect the cost of processing. ASFA does not support the use of high exit fees (penalties) as a means of discouraging members from leaving the fund. The issue of fees may, however, become more complicated for funds and members if portability is introduced without choice.

Most funds apply differing administration charges to active and inactive member accounts, but a standard exit fee. Creating a new class of exiting member (a partial active-account exit) may require funds to establish new (higher) exit fees to recognise the different processing costs. (Rather than closing an account, the fund process will include the transfer, updating of the member record to reflect the individual benefit components transferred, recording that this is a Regulation 6.33 request etc.) In this situation the introduction of portability without choice, rather than increasing competition and reducing fees across the industry, may have the opposite effect.

Combined with duplication of administration fees, these higher exit fees may in fact serve to negate any perceived benefit to the member arising from the ability to transfer current balances. In the absence of an explanatory memorandum with the exposure draft it is difficult to determine whether the government has undertaken a regulatory impact analysis and recognised the costs of a 'portability only' policy to both fund members and superannuation funds.

ASFA does not support the introduction of portability provisions without choice of fund.

Specific comments on the exposure draft regulations

The following comments relate to specific provisions in the draft regulations.

Superannuation Industry (Supervision) Amendment Regulations 2003

Terminology

Throughout the draft regulations the terms "rollover" and "roll over" are used. These are defined terms in the SIS Regulations. Our understanding is that "rollover" and "roll over" relate to the movement or payment of benefits where a member has satisfied a condition of release as listed in Schedule 1 of the SIS Regulations.

The correct term to describe what is proposed under the new Division 6.5 would appear to be, in all instances, "transfer".

In some schemes there may be a link between an accumulation benefit and a defined benefit paid on TPD. There does not appear to be a capacity, for contingency benefits to be reduced by the amount of a transfer requested under proposed Division 6.5. This has the potential to create a situation where a member with a TPD benefit that is a multiple of salary could have a sudden and potentially significant insurance increase that needs to underwritten. This would create the potential for increases in insurance premiums in excess of current employer contributions.

Item [3]
1.03B Meaning of protected member
It is noted (1.03B(3) that a person who exercises their rights under proposed Division 6.5 is not a protected member of the fund from which the amount was rolled over.

Although these members are not 'protected members', it is assumed that funds may still treat these members as 'protected members' where the fund trustee determines that such a policy is in the best interests of the members of the fund as a whole.

Item [6]
6.30 Application
Draft reg 6.30 states (6.30(2)(b) that division 6.5 does not apply to a SMSF. As Division 6.5 deals with rollovers and these, and transfers, are, by definition, transactions **between** complying superannuation funds, ADFs and RSAs, does the SMSF exclusion imply that a Division 6.5 roll over/transfer cannot be made to an SMSF?

A better form of words is needed in Draft reg 6.30(2)(c). As currently written it is subject to numerous interpretations such that the intent of the exclusion is not clear. This is another area where an exposure draft EM would have been of assistance, both in understanding the provision and in proposing more appropriate wording.

6.31 Definitions for Division 6.5
***Unfunded public sector superannuation* scheme**
It appears somewhat inefficient to have a definition at Regulation 6.31 which points to another provision in the regulations (Regulation 6.20B(5) when that other provision points to a separate piece of legislation (Regulation 2A of the *Superannuation Contributions Tax (Assessment and Collection) Regulations 1997*.)

Why not just repeat the Regulation 6.20B(5) definition?

6.31 (2)

It is noted that the definition of **defined benefit component** is identical to that used elsewhere in SIS. However, the examples included at 6.31((2)(a)(iii) are typically members of funds that are excluded from the operation of the division by 6.30(2)(a).

It is suggested that a more appropriate example be included, or the example given removed.

6.31(3)
Can this wording be improved?
The following wording may work:

> For the purpose of subregulation (2) a benefit that is only payable on death or disability is not a *defined benefit component.*

6.33 Request for rollover of withdrawal benefit
As this is, from both the member's and the fund's perspective, the main operating provision, 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.

An additional subregulation detailing the type of information required may assist.

The additional subregulation could be either general (e.g. sufficient information to enable the trustee to undertake the transfer including the amount to be transferred and the destination of the transfer), or specific (e.g. the ABN of the destination fund, the amount to be transferred out of the fund and either the SPIN of the destination fund/product or the members account number in that fund).

6.35 Rollover is subject to the receiving fund's rules
ASFA would question whether the term 'governing rules' is broad enough.

The restriction on acceptance of contributions and transferred amounts may not be in the actual governing rules but in supporting documents such as a prospectus. This would typically apply in the case of retail funds where, in the absence of an employer sponsor arrangement, minimum opening balances (initial contributions) may apply.

As worded it is conceivable that a fund would be required by regulation to make the transfer to a fund that was unable to receive it. The conflict arises through the inability of the receiving fund to provide the sending fund with a statement that their governing rules prevent receipt of the transfer.

6.36 Suspension or variation of obligation to roll over amounts by APRA

The terms 'on reasonable grounds' and 'significant adverse effect' (Regulation 6.36(1)) requires definition either through regulation or a Superannuation Circular issued by the Regulator **prior** to the provisions coming into effect.

In the absence of an exposure draft explanatory memorandum it is difficult to envisage, and comment on, the scope of application intended by the government.

Similar comments apply to draft Regulation 6.37(6) where the same term is used in reference to consideration by the Regulator of a superannuation funds capacity to meet a payment request.

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

Given the interrelationship between the provisions of Regulation 6.37 and Regulation 6.34, it would appear that, for the provisions to work effectively, there should be some time constraint imposed on a trustee wishing to avail themself of Regulation 6.37

As the provisions stand a trustee may, after receiving a valid application wait say 80 days before making an application to the regulator for relief. Although APRA has 30 days to respond, Regulation 6.34 would require the trustee to make the payment no later than the ninetieth day.

Regulation 6.34 does not grant relief to the trustee where relief has been **sought** under Regulation 6.37, only where relief has been **granted** under Regulation 6.37

ASFA suggests that a time limit (say within 30 days of receiving a request) be imposed on the ability for the trustee to apply for relief under this provision so as to avoid the conflict that may arise between the requirement to pay and the seeking and granting of relief due to an inability to pay.

Retirement Savings Accounts Amendment Regulations 2003

Item [3]

1.03A meaning of protected RSA holder

It is noted (1.03A(2) that a person who exercises their rights under Section 50 of the RSA Act, and specifically the proposed Regulation 6.15(2) right to transfer only part of their benefits is not a *protected RSA holder* of the RSA from which the amount was rolled over

Although these members are not *protected RSA holders*, it is assumed that the RSA provider may still treat these members as *protected RSA holders* where the RSA provider determines that such a policy is in the best interests of the members of the RSA as a whole.