

CHAPTER 1

INTRODUCTION TO THE INQUIRY

Background to the legislation

1.1 The Government's choice of fund policy is long standing and was originally announced in the policy platform for the 1996 election. The main objective of that policy was to provide greater freedom of choice for superannuation contributors and greater competition between funds. It is claimed that this may lead to reduced costs and increased returns.¹

1.2 The Wallis Committee, which was set up by the Government in 1996 to establish a common regulatory framework for overlapping financial products and to propose ways for dealing with further financial innovation, also recommended that superannuation fund members should have greater choice of funds.²

1.3 The Government described its choice of fund proposal in detail as part of the May 1997 Budget. The Government announced that it would introduce choice of fund for new employees from 1 July 1998, and extend choice to existing employees within two years of the date of effect of the legislation. Under the Government's proposal, employers were required to offer employees choice from among five or more complying superannuation funds or Retirement Savings Accounts (RSAs) nominated by the employer.

1.4 The Government announced changes to this policy on 25 November 1997, following extensive consultations with industry. Announcing the changes, Senator the Hon. Rod Kemp, the Assistant Treasurer, said that the 'enhancements' would:

...improve the choice arrangements by significantly reducing the administrative burden on employers while ensuring the key objective of providing choice of fund to employees is achieved.³

1.5 The major changes to the original policy were as follows:

- limited choice of five funds reduced to four; and
- introduction of a new 'unlimited employee choice' option.

¹ Superannuation and the Budget: Policy Development for the Next Century, a paper presented to LIFA by David Connolly MP, Shadow Minister for Superannuation and Retirement Incomes, 25 May 1995.

² *Financial System Inquiry – Final Report*, May 1997, Chairman Mr Stan Wallis (the Wallis Report), Recommendation 88, p.62.

³ Assistant Treasurer, Press Release AT/23, 25 November 1997.

1.6 On 4 December 1997, the Government presented Taxation Laws Amendment Bill (No. 7) 1997 in the House of Representatives. Schedule 5 of the Bill consisted of a series of amendments to the *Superannuation Guarantee (Administration) Act 1992*, the *Retirement Savings Account Act 1997* and the *Superannuation Industry (Supervision) Act 1993*, that were intended to give effect to the Government's proposal.

1.7 Briefly, the amendments required employers to make compulsory superannuation contributions (SG contributions) to a complying superannuation fund or RSA account in accordance with the choice of fund requirements. A higher rate of SG charge was to be levied on employers who did not comply with those requirements. Choice of fund was to apply to new employees from 1 July 1998 and to existing employees two years later.

Previous Committee's report

1.8 The former Select Committee on Superannuation examined the proposed legislation in its twenty-eighth Report to the Senate, entitled *Choice of Fund*, tabled in March 1998.⁴

1.9 There was deep division on the timing for the introduction of choice between those groups favouring adherence to the Government's announced schedule and those who advocated delay. The former group included banks, some specialist service providers and some of the major life companies who had products ready for the introduction of choice and were confident they could complete prerequisites, such as Key Features Statements, before 1 July 1998.

1.10 The latter group, which included the Association of Superannuation Funds of Australia, consumer and legal advocates, some major employers, small employers and many of the major consulting groups, expressed concerns about a number of issues. These concerns included the level of education about choice, the preparatory work necessary and the cost of implementation of a choice regime, the adequacy of consumer safeguards, differing federal/state applications and the cost of distribution and the impact on the fund members' final retirement income.

1.11 It was widely accepted that 'informed' choice was necessary if the choice proposal was to be successful, with the two key requirements being education of consumers and employers and adequate disclosure of comparable information about funds.

1.12 Employers, especially small employers, needed education about their obligations, responsibilities and options and employees needed sufficient information about their rights and how to make a sensible choice. It was felt that Key Features Statements should contain educational material which discouraged people from

⁴ Senate Select Committee on Superannuation, Twenty-eighth Report, *Choice of Fund*, Canberra, March 1998.

exercising choice of fund until they had adequately informed themselves of the consequences of changing funds and understood what alternatives were being offered to them.

1.13 On the issue of disclosure, it was felt that Key Features Statements should clearly indicate the consequences of choosing a particular fund, including the adequacy and coverage of insurance, the costs associated with switching funds, and the relative risks associated with each option offered.

1.14 The selection of a default fund for the contributions of those employees who chose not to exercise choice, and the principles and standards which should govern such a fund, were a topic of concern for some witnesses.

1.15 Employee advocates and consumer groups were concerned about the level of consumer protection to be offered under choice, including the need for arbitration of any disputes arising between employers and employees in matters relating to choice of fund.

1.16 It was widely recognised that a choice regime would represent very significant change to administrative arrangements for superannuation. While some groups advocated proceeding with choice speedily, others felt that a delay of at least a year would be prudent to enable all the concerns noted above to be adequately addressed.

Status of the legislation

1.17 In the event, Schedule 5, containing the choice of fund provisions, was deleted from the Taxation Laws Amendment Bill (No. 7) 1997 to ensure timely passage of other measures in that Bill and because the Government did not have support for its choice proposals. The choice legislation was reintroduced on 12 November 1998 as the Superannuation Legislation Amendment (Choice of Superannuation Funds) Bill 1998.

1.18 The legislation provides that an employer is required to offer an employee either of two options, either a 'limited choice' offer; or an 'unlimited choice' offer. A limited choice offer enables the employee to select a chosen fund from a choice of at least four eligible funds nominated by the employer. An unlimited choice offer enables the employee to select any eligible choice fund as his or her chosen fund.

1.19 The legislation also makes provision for a default fund into which an employee's contributions may be placed while he or she is choosing a fund, or when an employee does not have a chosen fund and does not choose one when given a chance. Contributions to unfunded public sector schemes; contributions made in respect of employees covered by Australian Workplace Agreements and certified agreements under the Workplace Relations Act; and contributions in accordance with State industrial awards are also deemed to satisfy the legislation.

1.20 The House of Representatives passed the latter Bill on 16 February 1999. However, debate on the Bill in the Senate was adjourned on 17 February 1999 and the Bill remains on the Table for consideration.

Developments since the previous report

1.21 In the two years since the draft legislation was originally formulated, conditions in the financial sector in general and in the superannuation industry have continued to change.

- Convergence in the financial industry, with large entities increasingly offering consumers the full range of financial services – banking, insurance and superannuation products – has blurred the demarcation lines which formerly existed in the financial sector.
- The proportion of Australians with direct exposure to the share market has continued to rise. A recent ASX survey shows a significant increase in the level of share ownership, from 32 per cent of the Australian adult population in October 1998 to 41 per cent in November 1999. The listings of AMP in June 1998 and the second Telstra float in October 1999 between them added over a million first time investors to Australia's share market. In addition, many more young people are entering the sharemarket – of the 5.7 million Australians who now own shares directly, some 1.5 million are aged between 18 and 34 years.⁵
- A significant number of funds at their own initiative have offered investment choice, that is, a range of products with different levels of risk and return, within one superannuation fund. Some are also offering choice of the types of industry or activities in which the superannuation monies are invested.
- Queensland, New South Wales and Western Australia have introduced different models of employer/employee choice under state legislation. The most recent instance was the commencement of employee choice of fund in Western Australia on 1 July 1998 under state industrial legislation, which came into operation on 1 January that year.
- Rising levels of superannuation savings and an increased level of financial knowledge among consumers may be beginning to influence consumer sentiment on superannuation. Some recent surveys suggest that consumers want more 'ownership' of their retirement savings. An Australian Consumers' Association survey of financial issues in February 1999 found that 83 per cent of respondents currently contributing to a superannuation fund were in favour of allowing people to have a choice of fund.⁶ A recent AC Nielsen survey found a similar level of support.⁷ However, these results are in stark contrast to the most

5 *ASX News Release: Share Ownership 2000*, 8 February 2000.

6 Submission No. 12a, p. 2.

7 Submission No. 9b, p 1.

recent ASFA survey conducted by Worthlin Worldwide Research which indicated that choice is a low-order priority well below issues of security and simplicity, which rank as the most important reform priorities for fund members.

Roundtable initiative

1.22 Mindful of its brief to inquire into matters pertaining to superannuation and financial services, including ‘prudential supervision and consumer protection for superannuation and financial services’, the Select Committee on Superannuation and Financial Services decided to conduct a ‘round table forum’ on the subject of choice.

1.23 The aim of the meeting was to provide the Committee with an opportunity to identify, with the assistance of key individuals and organisations, the best features that might be considered in any future choice of funds regime.

1.24 The roundtable meeting took place in Sydney on 14 December 1999 and the proceedings are briefly described in the following chapter. A list of those who participated in the forum appears at Appendix 1. A list of submissions made to the inquiry is at Appendix 2.

