

CHAPTER 8

INVESTMENT CHOICE

Introduction

8.1 The issue of investment choice has been discussed for some time. In the previous Committee's 1998 report on *Choice of Fund*, industry bodies contended that investment choice was a good platform from which to proceed with the choice of fund.

8.2 At the 1999 roundtable, many participants referred to the relevance of the investment choice experience to date as being a pointer to how choice of fund will operate in its early stages.

8.3 Investment choice generally refers to a differentiation of investment streams within any one superannuation fund, that is, the provider offers a range of products with different levels of risk and return. Investment choice also allows member assets to be invested in industries and activities the member considers morally, socially or economically desirable.¹

8.4 Investment choice products based on different risk and return profiles are generally distinguishable by the names given to the products by providers. Three basic descriptions are:

- Capital guaranteed funds;
- Balanced funds; and
- Growth funds.

8.5 This type of choice is a service being provided by an increasing number of funds. While some point to the cost of investment choice as significant², as mentioned in Chapter 5, a number of providers are using the e-commerce mechanism as a means of lowering that cost.

Take-up rate

8.6 At the 1999 roundtable, industry sources claimed that the number of members using the option of choice of investment is increasing. Evidence to the Committee

1 *Choice of Fund*, (1998) p. 23.

2 Submission No. 15, p. 8.

indicated that around 20 per cent have taken up the option when the choice is offered.³ However, the actual take-up rates varied among funds that offer investment choice.

8.7 Jacques Martin Industry Funds Administration advised that it has around 2.6 million superannuation accounts, and offered member investment choice to most of those people inside their accounts. It found that only around 15,000 people made a deliberate choice.⁴

8.8 The ACTU reported that over 1,000 people have exercised choice out of 350,000 members, or 150,000 to 200,000 active members.⁵

8.9 Some funds indicated that investment choice was offered to a particular class of member. For example, Westscheme offered choice of investment to 4,000 members who had account balances over \$10,000 which resulted in 600 members exercising choice.⁶

8.10 AMP Financial Services estimated that 20 – 25 per cent of people in its funds, had taken up the opportunity to use investment choice.⁷

8.11 It was suggested by Jacques Martin Industry Funds Administration that the take-up rate of internal member investment choice within a fund ‘would be a good measuring stick (for the launch) into an open choice of fund environment.’⁸

8.12 In evidence to the Committee, witnesses commented that the reasons behind the apparent slow take-up included:

- the lack of awareness and education in relation to the range of investments available; and
- the possible costs involved in switching between investments; and
- an individual’s account balance.

These issues are discussed below.

Education

8.13 While the number of people exercising choice of investment has increased over time, evidence to the Committee suggested that the quality and quantity of education is a factor affecting the rate at which people exercise choice. When

3 Submission No. 15, p.8.

4 Hansard, p.11.

5 Hansard, p. 75.

6 Hansard, p. 62.

7 Hansard, p. 59.

8 Hansard, p. 11.

considering the factors that prompt people to make a choice, AMP Financial Services stated that ‘education is the greatest influence.’⁹

8.14 AMP Financial Services also advised the Committee that it has a very substantial program that it provides free to the employer sponsor for their members which is purely on an educational, information basis:

This is purely on the basis of an education in assisting people to understand what investment choice is about: the risk component of investment, where they sit as an investor and where they are comfortable. It extends beyond just the investment choice and understanding of investment markets. It also helps them to understand how much they need to save for retirement in terms of adequacy. It covers issues on health. So it is a broad range of education programs which we have put into place.¹⁰

8.15 Evidence to the Committee suggested that those funds that offer face-to-face advice achieve higher returns. For example, AMP Financial Services advised that it offers education in the form of face-to-face consultations and seminars, and that in those funds where employer sponsors have taken up the opportunity for this service, ‘about 70 per cent of members of those funds attend the seminars.’¹¹

8.16 In contrast, Westscheme advised that when it distributes welcome letters to new members with tear-off slips telling them about the information they can get from us, ‘we do not get a huge number of those coming back.’¹²

8.17 While education is the greatest influence, AMP Financial Services agreed that various other factors appear to act as triggers to choice, including age, accumulation of superannuation assets, income and the amount of years left to retirement. While the young seem to be relatively uninterested in superannuation, those closer to retirement age have a greater interest in maximising their retirement income.¹³

Costs

8.18 Witnesses advised that the take-up rate of investment choice has also been influenced by the possible costs involved in switching between investments.

8.19 However, in evidence to the Committee, the Australian Retirement Income Streams Association advised that it is aware of some funds that offer a certain number of free switches:

9 Hansard, p. 63.

10 Hansard, p. 58.

11 Hansard, p. 59.

12 Hansard, p. 65.

13 Hansard, pp. 62-63.

In the retirement income area, and we would be talking usually about larger sums of money there, most publicly offered funds would offer a certain number of free switches per year and then, after that, the member would start to pay a fee for the switch.¹⁴

8.20 The Committee was advised that other funds may provide a similar service and that with respect to subsequent switches, fees are charged in a range from \$20 upwards. For example, in its guide to consumers, the Accountants Superannuation Fund Nominees Pty Ltd advertise that 'there is no charge for the first change each year; however additional charges in the same year will cost \$20.'¹⁵

8.21 William M Mercer Pty Ltd, advised that, based on its experience in the USA, switching activity is a lot lower than people anticipate.¹⁶

8.22 In evidence to the Committee, the Association of Superannuation Funds of Australia noted one example of the implementation costs for a corporate Fund (with about 4,200 members) 'amounted to some \$500,000 or \$120 / \$130 per member.' In this example the costs were borne by the corporation rather than the fund members however, this will not always be the case.¹⁷

Account balance

8.23 Witnesses also advised the Committee that another reason for the apparent slow take-up rate was that people would not generally be interested in investment choice until they had accumulated a reasonable balance in their accounts.

8.24 Both the AMP Financial Services and William M Mercer Pty Ltd advised that 'account balance' was one of the factors influencing investment choice. The latter company explained that '...people with higher account balances are more likely to respond.'¹⁸

Summary

8.25 Overall the evidence suggests that:

- The options for investment choice are increasing, but the take-up rates vary among funds that offer investment choice;
- The main reasons behind the apparent slow take-up rate relate to lack of awareness and education in relation to the range of investment available; the possible costs involved in switching between investment and account balance.

14 Hansard, p. 60.

15 Accountants Superannuation Fund Nominees Pty Ltd, *Guide*, November 1999.

16 Hansard, p. 61.

17 Submission No. 15, p. 8.

18 Hansard, pp. 62-63.