Treasury Laws Amendment (Improving Accountability and Member Outcomes in Superannuation Measures No. 2) Bill 2017

SCHEDULE 1 (CHOICE OF FUND PROVISIONS)

29 September 2017

Industry Super Australia

ABOUT INDUSTRY SUPER AUSTRALIA

Industry Super Australia (ISA) is an umbrella organisation for the industry super movement. ISA manages collective projects on behalf of a number of Industry SuperFunds with the objective of maximising the retirement savings of five million industry super members. Please direct questions and comments to:

Matthew Linden
Director of Public Affairs
[redacted]

Phil Gallagher PSM
Special Retirement Policy Adviser
[redacted]

Richard Watts
Consultant
[redacted]

ISA Pty Ltd ABN 72 158 563 270 Corporate Authorised Representative No. 426006 of Industry Fund Services Ltd ABN 54 007 016 195 AFSL 232514

TREASURY LAWS AMENDMENT (IMPROVING ACCOUNTABILITY AND MEMBER OUTCOMES IN SUPERANNUATION MEASURES NO. 2) BILL 2017

Contents

1. Members exercising choice of fund are not well protected 4

2. The Government's estimates of affected employees are inflated 7

2.1 Number of impacted employees in operating enterprise agreements 7

2.2 Misinterpretation of superannuation clauses in enterprise agreements 8

2.3 ISA analysis of data shows limitations on choice are very rare 8

2.4 Special characteristics of workplaces where limited choice exists 10

2.5 Measures to reduce and mitigate non-payment of superannuation contributions 11

2.6 Payment of additional superannuation contributions 12

2.7 Insurance arrangements 13

2.8 Funds named in EBAs have provided superior member outcomes. 14

3. Safeguarding member outcomes 15

3.1 Retirement decisions are complex 15

3.2 Low levels of financial literacy in Australia 15

3.3 Navigating 'Choice' 17

4. Requirements for informed choice 18

4.1 Choice must be informed 18

4.2 Different Product disclosure regimes a 'fee-asco' 19

4.3 Choice dashboards 19

4.4 Different regulatory approach to choice and non-choice products 20

Attachment 1 – Rice Warner Report (Member Switching) 22

Figures

Figure 1 – When members exercise “choice of fund” they pay higher fees, predominantly in retail funds 5

Figure 2 – Aggregate increase and decrease in fees paid by sector $Millions, 30 June 2015 5

Figure 3 – Members switched into funds that had, on average, lower net returns 6

Key points

- Industry Super Funds support a regulatory framework that provides for a strong default fund safety net, combined with strong consumer protections that prioritise members, together with clear and complete information to make informed decisions.
- "Choice of fund" sounds superficially attractive, but will lead to millions of dollars in consumer harm if it is not accompanied by strong consumer protections and enforcement. So far, academic research about what happens to consumers when they choose their own fund clearly shows that policy makers have let consumers down. Policy makers have exposed members to finance sector sales without insisting on consumer friendly disclosure and iron-clad protections around the sale of financial products. Schedule 1 of this proposed Bill repeats that mistake.
- The proposed Choice of Fund provisions in Schedule 1 of the Bill are being advanced despite woeful consumer protections:
  - New research from Rice Warner shows that when members choose their own fund, they usually choose funds with *higher* fees, not lower fees. They usually choose funds that have *lower* performance, not higher performance. And they usually choose retail super funds.
  - While there is a small percentage of people who care a great deal about where their super contributions go, most people who choose a fund do so only after they are "sold" a product such as by a bank teller, or a financial planner. Therefore, the sales practices for superannuation must be iron clad, be free of conflicts, and put members first.
  - Current disclosure rules, and new ASIC regulatory guidance regarding fee and cost disclosure, make it difficult if not impossible to easily understand and compare superannuation products. Indeed, new ASIC guidance entrenches a two-tiered disclosure regime in which direct and indirect investment costs are disclosed in conventional super fund product disclosure statements, but platform superannuation products do not need to include indirect costs in the PDS. Platform superannuation products are the predominant way retail super funds offer superannuation, meaning that this new guidance effectively has a different regime for most retail products.
  - Newly proposed disclosure rules regarding portfolio holdings in Treasury Laws Amendment (Improving Accountability and Member Outcomes in Superannuation Measures No. 1) Bill 2017 also expressly exclude platform products. Again, this means the disclosure to members is not only incomparable between conventional superannuation and platform superannuation, but that the level of transparency for platform options (i.e., most retail products) would be lower.
  - Newly proposed requirements for trustees to assess the value-for-money of the super products they offer expressly apply only to MySuper products, not choice products (see Treasury Laws Amendment (Improving Accountability and Member Outcomes in Superannuation Measures No. 1) Bill 2017). Choice products currently have much lower average performance compared to MySuper or default products. Omitting choice products from these requirements continues to expose members to risks of lower long term returns and higher fees when they choose their own fund, undermining retirement security.
  - Following lobbying by bank owned and retail super funds, Choice Product Dashboards have been deferred a total of 5 years beyond their original commencement date on 1 July 2014, further undermining the ability of individuals who are comparing choice products to make informed comparisons of fees costs and returns.
- The Government's estimates of the number of workers who are in Enterprise Agreements that do not provide already choice of fund is highly inflated, overstating the case for change and undermining the

credibility of the position. As explained in Section 2.4, the percentage of the workforce with no choice of superannuation fund is about 186,000 people, or just *1.9 per cent of all employees*.

- While not common, there are Enterprise Bargaining Agreements that restrict choice. These arrangements are more common in (1) in construction and other industries with higher risk of unpaid superannuation, because a requirement to make super contributions under the agreement into only one fund assists with compliance monitoring, and (2) the retail sector of the economy, where EBAs provide superannuation to many workers who would not otherwise receive it because they are below 18 or earn under the $450 threshold.
- Superannuation funds named in Enterprise Bargaining Agreements have delivered above average long term net returns to members. The superannuation terms of these agreements reflect the voted-for position of workers. They have also reduced employer compliance costs. As a result, the Bill creates significant trade-offs that have not been responsibly considered.
- The Government has not analysed the costs and benefits of its proposals to inform Parliament.

ISA recommends that the Committee reject Schedule 1 of the Bill as proposed and insist the Government:

1. **Immediately implement measures to provide appropriate consumer protections to protect members who switch or choose a fund, including reversing the five year delay to the commencement of Choice Product Dashboards, and**
2. **Development an appropriate fact base and assessment of the cost and benefits of the proposal.**

Executive Summary

Industry Super Funds support a regulatory framework that provides for a strong default fund safety net, combined with strong consumer protections that prioritise members, together with clear and complete information to make informed decisions.

For over a decade, since the introduction of choice of fund, industry super funds have, collectively and individually, been active market participants.

However, policy makers need to take seriously that "choice of fund" is merely a diplomatic way of saying "superannuation sales". While there is a small percentage of people who care a great deal about where their super contributions go, most people who choose a fund do so only after they are "sold" a product such as by a bank teller, or a financial planner.

Put another way, the vast majority of people who choose a super fund do so under the influence of sales strategies by the finance sector. And individuals facing sales strategies generally do so with relatively low financial literacy.

It doesn't do anyone – other than, of course the big banks and the finance sector – any good to promote choice of fund without clear, comparable and consumer-friendly disclosure. Perhaps more importantly, this disclosure must be accompanied by strong and aggressively enforced rules requiring those who sell superannuation to do so in in a way that prioritises the best interests of members. Although the Future of Financial Advice Reforms do apply a best interest duty for personal advice, general advice by bank staff are not subject to these rules, in addition to other carve outs. There also are questions regarding FOFA enforcement.

Appropriate consumer protections are essential accompaniments for choice of fund. Without them, policy makers cannot have a clear conscience – they have delivered vulnerable consumers into a sales environment without fair information and without fair protections.

Today, the disclosure rules in superannuation are a far cry from consumer friendly.

And the sales practices are clearly harming consumers. New research by Rice Warner – consistent with multiple academic research papers – shows that when members choose their own fund, they tend to make poor decisions. Overall for those that choose they end up in funds with *higher* fees, not lower fees. They end up in funds that have *lower* performance, not higher performance. And for the vast majority they gravitate to retail funds. Despite holding just under 40 percent of APRA regulated assets they account for 72 percent of switches by value. In fact, 92 per cent of the net increase in fees that occurred when people chose to switch to a new fund, were paid by people who switched to a retail fund.

How can this completely irrational and harmful, outcome happen? Because banks and retail funds, and their political allies, do not support choice of fund out of the goodness of their hearts. It is no coincidence choice of fund is accompanied by woefully inadequate consumer protections.

The proposed Bill would help the relatively small number of people who care deeply about where their super contributions go, and are in an enterprise agreement that restricts choice of fund. But the proposed Bill is not about this tiny number of people. The real outcome of this Bill is it would further expose the millions of workers who are in a good super fund due to their enterprise agreement to the selling pressures of the finance sector. And it would expose them to these selling pressures without adequate information and without appropriate consumer safeguards.

We note that the other Bills introduced by the Government regarding superannuation include a number of express carve-outs for choice products from consumer protections and disclosures. This is no accident.

The finance sector see members' super savings as a source of profit for themselves. For them consumer protections get in the way.

This Parliament has the opportunity to do better than it did in 2005-6, when choice of fund was introduced. This time, policy makers can insist on iron clad protections. The Parliament should not support proposals that expose members to finance sector sales while carving out choice products from consumer protections.

The Government is rushing these super reforms. Insisting on consumer protection that is effective and is based on well-drafted laws is not achievable in the 11th hour of an accelerated legislative process.

The Parliament should put members first, not the finance sector. This means sending the Bill back to Government for further consultation to:

- Provide appropriate consumer protections. Such protections need to ensure clear and consumer-friendly disclosure of performance as well as fees and costs. For example, superannuation platforms (which are where the majority of retail fund assets rest) are now subject to a different disclosure regime than conventional super products, which is harder to navigate for members.
- Provide an appropriate fact base and assessment of the cost and benefits of the proposal. Indeed, the government's purported number of people who are in Enterprise Agreements that do not permit choice of fund is grossly inflated according to analysis of the Department of Employment's Enterprise Agreement dataset.

1. Members exercising choice of fund are not well protected

A number of academic papers have shown the members exercising choice of fund are harmed. Specifically, they end up poorer than they otherwise would be.[1]

New research by Rice Warner[2] dives into this question using APRA data and draws upon 10 million members' annual statement data.

Rice Warner looked at super fund rollover and switching behaviour – what members were switching funds, where they switched to, and what happened to them.

The report found the aggregated *net* impact (balancing out gains and losses) of changing funds undermines system efficiency, because it resulted in *a $137 million increase in fees*; and a *$284 million decrease in investment performance* per annum.

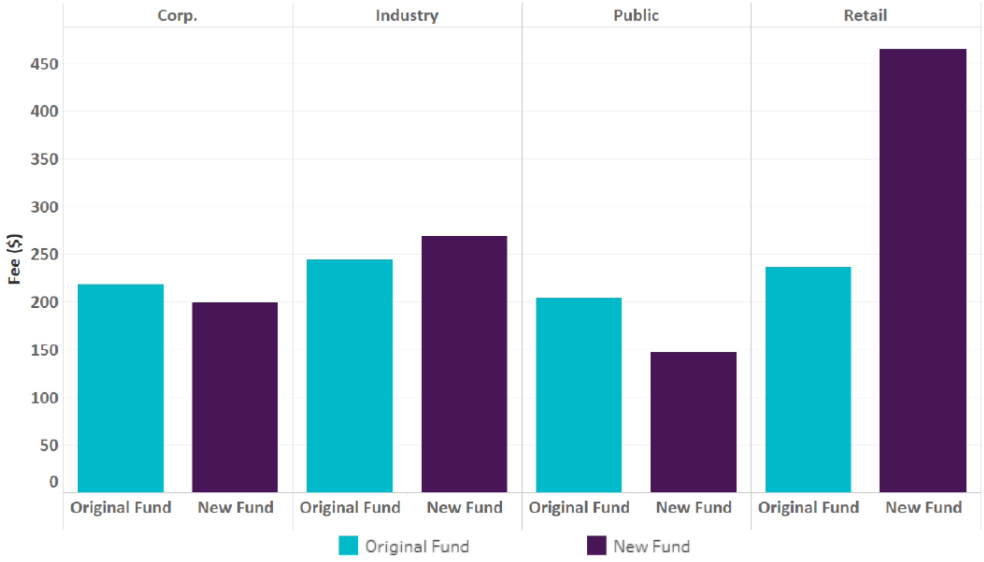
Figure 1 shows the effect of switching on fees by sector, and Figure 2 shows the aggregated increase and decrease in fees by sector.

[1] Delpachitra, Sarath and Rafizadeh, Schumann, *The Switching Decision: Are Members of Superannuation Funds Rational and Informed Investors?,* Australasian Accounting, Business and Finance Journal, 8(4), 2014, 45-62. Available at:http://ro.uow.edu.au/aabfj/vol8/iss4/4

Agnew, Julie R.; Bateman, Hazel; and Thorp, Susan (2013) "Financial Literacy and Retirement Planning in Australia," Numeracy: Vol. 6: Iss. 2, Article 7. Available at http://scholarcommons.usf.edu/numeracy/vol6/iss2/art7; also see the work of Iyengar, S. S, and Lepper, M. R, 'When Choice is Demotivating: Can one Desire too Much of a Good Thing?', Journal of Personality and Social Psychology, 79(6), 995, 2000 and Iyengar, S. S., Huberman, G., & Jiang, W, How Much Choice is too Much? Contributions to 401 (k) retirement plans. Pension design and structure: New lessons from behavioral finance, p 83–95

[2] Rice Warner, Member Switching, September 2017 http://www.industrysuperaustralia.com/assets/Uploads/Rice-Warner-Industry-Super-Member-Switching-180917-FN.pdf

Figure 1 – When members exercise "choice of fund" they pay higher fees, predominantly in retail funds

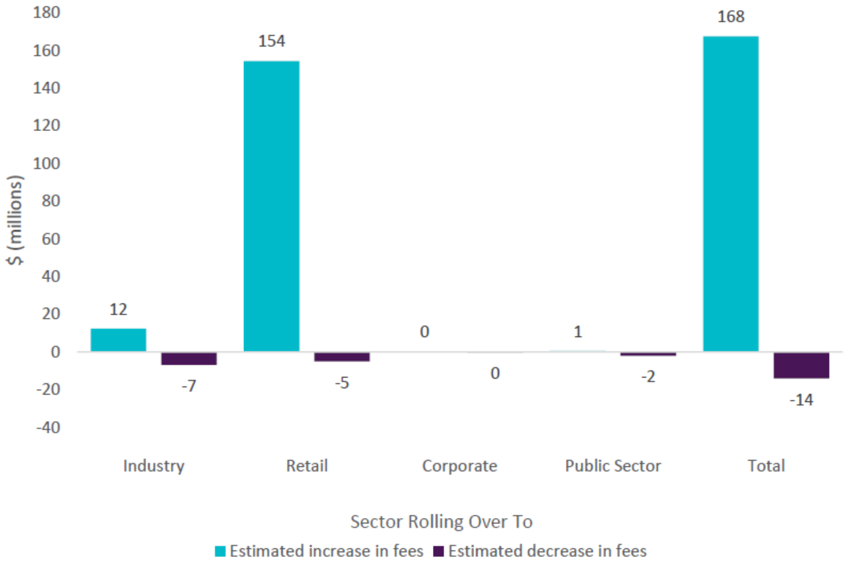


*Retail employer plans have been excluded from analysis as the level of discount provided is unknown. Hence the 'Retail' sector represents personal superannuation products only.

Source: Rice Warner
Note: For the year ending June 2015

More startling, however, is that, across the system (industry, public sector, retail funds) the estimated increase in super fees from switching was $170 million, of which, a staggering *$157 million* or *92 per cent* was in the *retail sector* (Figure 2).

Figure 2 – Aggregate increase and decrease in fees paid by sector $Millions, 30 June 2015

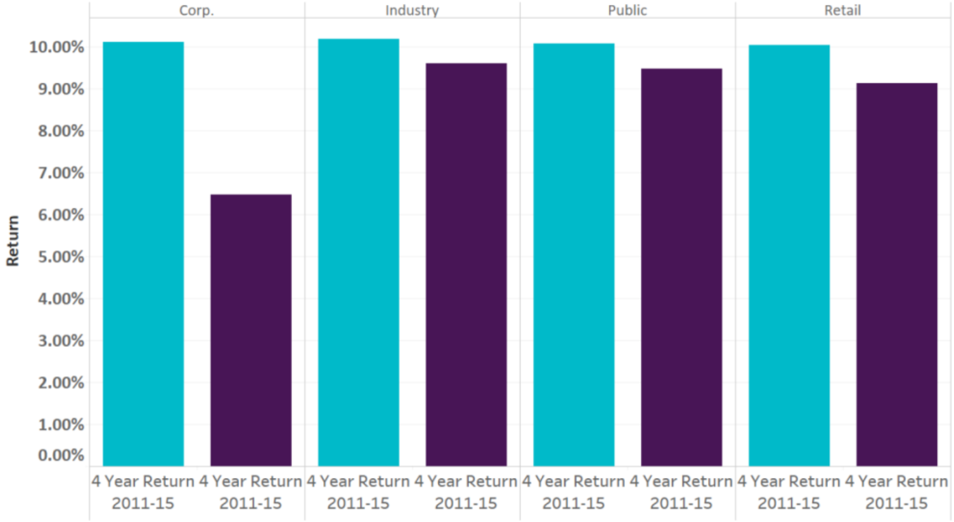


**Retail fee decreases do not include the decreases from rolling over into Retail Corporate Plans, due to the practice of providing discounts to PDS rates.*

Source: Rice Warner

Members not only choose to switch into (or, more accurately, are *sold* into) funds with higher fees, they also switch into funds that generated lower net returns than they would have had if they had not switched funds (Figure 3).

Figure 3 – Members switched into funds that had, on average, lower net returns



**Light blue represents the members' original fund and dark blue represents the fund rolled over to.*

Source: Rice Warner

Note: Difference in historical returns for those members moving to a fund with lower 4y returns

Overall, the key findings of the research were that:

- Just under 1 million Australians switched super funds in 2014-15 with more than half paying higher fees and switching to funds with lower returns
- Australians paid an estimated additional $170 million in fees after switching super funds
- Of those additional fees, 92% or $157 million was in retail funds; $12 million or 7% was in industry funds
- Retail super funds are the main switching destination accounting for 72% of all switches
- Retail super funds account for 92% of those members switching to a fund with higher fees
- Of members switching from industry to retail funds only 7% paid lower fees.
- Members rolling into industry funds are generally twice as likely to pay lower fees than those rolling into retail funds (21% against 9%).
- Retail funds accounted for 87% of decreases in investment returns.
- The net impact of changing super funds was a $137 million increase in fees p.a.
- Net impact of changing funds is a $284 million decrease in investment performance p.a.

A full copy of the report is provided as Attachment 1.

One of the main reasons members are switching funds in ways that harm their retirement security is because of sales tactics of bank-owned super funds. Detailed analysis by Roy Morgan Research shows that there has been a sharp increase in members switching to bank owned super funds who have received direct advice from the institution. This rate has almost doubled[3] among the big four banking groups between 2011 and 2015. Roy Morgan research shows that members are being switched out of funds with high net satisfaction and performance (often Industry Funds) into bank group funds with lower net satisfaction and performance. This is not a result that would be expected in an informed or competitive market.

2. The Government's estimates of affected employees are inflated

The Government's estimates of the number of Australian employees who as the result of being subject to the terms of an enterprise agreement do not have a choice into which employer superannuation contributions are made has varied. In December 2016 Minister O'Dwyer claimed that an estimated 800,000 Australian employees who are covered by Enterprise Agreements do not have the ability to choose a superannuation fund.[4] In the Minister's second reading speech introducing this Bill the impacted employees had purportedly grown to 1 million.[5] Whilst the Bill's Explanatory Memorandum appears to rest on 700,000.[6]

At paragraph 1.48 of the Bill's Explanatory Memorandum it is claimed that as of June 2014 there were approximately 2.5 million employees covered by enterprise agreements. It is purported that a sample by the Department estimates that around 30 per cent or 700,000 of employees subject to enterprise agreements faced some restriction on choice of fund.

2.1 Number of impacted employees in operating enterprise agreements

It is important to note that not all employees covered by enterprise agreements are eligible for superannuation guarantee contributions. ISA estimates that for the 2013-2014 financial year 89.74 per cent of employees[7] were entitled to superannuation guarantee contributions.

A degree of caution also needs to be taken when analysing historical enterprise agreement data. Whilst enterprise agreements remain in force until replaced, the most common duration of enterprise agreements is three years. Care needs to be taken when relying on data which is in excess of three years. The data referred to in the Explanatory Memorandum in exceeds this time frame.

[3] The report shows that the growth in direct sales advice has corresponded with an increase in switching gains by the big four banking groups from 23.2 percent of the switching market in the 2011 report to 32.6 percent of the switching market in the 2016 update which represents a 41% increase in switching gain market share.

[4] Media Release The Hon Kelly O'Dwyer MP Minister for Revenue and Financial Services, 10 December 2015

[5] Hon Kelly O'Dwyer MP Minister for Revenue and Financial Services, 14 September 2017. Second Reading Speech Treasury Laws Amendment (Improving Accountability and Member Outcomes in Superannuation Measures No. 2) Bill 2017; "….. , it is estimated that around a million people are covered by federal enterprise bargaining agreements that restrict their ability to choose their own fund. "

[6] Treasury Laws Amendment (Improving Accountability and Member Outcomes in Superannuation Measures No. 2) Bill 2017; Explanatory Memorandum paragraph 1.48

[7] Using 2013-2014 ABS Employee estimates.

The Bill and Explanatory Memorandum correctly recognise that there are categories of employees to which choice of fund will not apply; these include existing members of defined benefit schemes and members of certain public sector schemes.[8]

2.2 Misinterpretation of superannuation clauses in enterprise agreements

The Government appears to be operating on the misapprehension that the naming of a specified default fund within an enterprise agreement extinguishes choice. This is not the case. Very few enterprise agreements restrict choice of superannuation fund to a single fund or list of named funds and fewer again do not provide for choice of fund.

The naming of a fund within an enterprise agreement per se does not remove an employee's right to nominate a superannuation fund of their choice to receive employer superannuation contributions. At 1.49 of the Explanatory Memorandum the following is stated:

> *1.49 If an enterprise agreement provides for contributions to be paid to a particular fund or to one of a limited list of funds, then the employer must pay those contributions to the fund(s), or risk breaching the agreement. The payment of contributions to the fund(s) is then deemed to be compliant with the choice requirements, meaning that if the employer contributes the appropriate amount to that fund within the correct timeframe, they will not be liable to pay a penalty. In these circumstances, individuals have no freedom to exclude themselves from the collective agreement and exercise their own choice.*

The mere naming of one or more superannuation funds in an agreement as a default does not extinguish employee choice. This fundamental error appears to be a possible explanation for the Government's inflated estimates.

Unless the terms of the relevant superannuation clause clearly remove choice, choice of fund for the employee remains. Some enterprise agreements do restrict choice to one or a number of funds. As a result of the bargaining process in some instances the choice is in the hands of employees and in other agreements with employers.

2.3 ISA analysis of data shows limitations on choice are very rare

ISA's analysis shows that the Government estimates of employees who do not have choice are grossly inflated. Research undertaken by ISA using enterprise bargaining data supplied by the Department of Employment clearly demonstrates that most employees have choice.

ISA's analysis shows that of those employees covered by enterprise agreements only 7.4 per cent have no choice of superannuation fund representing 1.9 percent of the workforce. The 17.8 per cent of employees that have a range or limited number of superannuation funds to choose from (including to right to choose an existing fund they may hold) represents only 4.5 per cent of the workforce.

The data clearly shows that the vast bulk of employees subject to an enterprise agreement or other relevant workplace determination do have the right to exercise choice of superannuation fund.

ISA has accessed the Department of Employment's enterprise agreement database and has used a stratified sample of all enterprise agreements that have an expiry date after December 2015. The sample includes all agreements with more than 90 employees covered by the terms of the agreement and a 7.5 per

[8] See 19(2B)(c).

cent sample of all agreements with less than 91 employees. The sample was weighted to give population estimates.

2.3.1 Detailed analysis

To the best of our knowledge ISA is the first party to undertake a detailed analysis of the superannuation terms within enterprise agreements. ISA has individually coded 2432 enterprise agreements to determine if the terms of the relevant superannuation clauses allow for superannuation choice or impact that choice in some way.

- Each relevant enterprise agreement clause was coded to determine if the clause:
- Limited the employee's choice of superannuation fund to a range of funds;
- Provided no employee choice of superannuation fund;
- Provided the employee choice of superannuation fund; and
- Offered a range of named defaults

ISA's detailed analysis was supported by legal and industrial relations subject matter experts.

Table 1: Estimated Employee Choice by Sector: Percentage of Employees with Enterprise Agreements Active in 2016

	Employee Choice			
Sector	**Limited**	**No**	**Yes**	**All**
Private	10.8%	6.8%	82.4%	100.0%
Public	6.8%	12.3%	81.0%	100.0%
All	10.3%	7.4%	82.2%	100.0%

Source: Source ISA coding of Stratified Sample of FWC Agreements also in the Department of Employment Enterprise Agreement dataset. Agreements selected (from many years) were active beyond 31 December 2015.

Only 7.4 per cent of employees have no choice of fund with 6.8 per cent in the private sector. Over 82 per cent of employees have no restriction within their enterprise agreement on the superannuation fund into which their employer will make superannuation contributions. ISA estimates that only 17.8 per cent of employees covered by agreements have some restriction on choice. This figure includes some public sector employees who will not be impacted by the Bill.

As few as 17.8 per cent of employees covered by agreements have some restriction on choice – including those in public sector schemes. Table 2 demonstrates that of those employees with limited choice, 26 per cent had more than one named default fund to choose from.

Table 2: Number of default superannuation funds named by Choice Status: Percentage of Employees Covered by Agreements

	Employee Choice			
Number of default Superfunds named in agreement	Limited	No	Yes	All
Zero	5.8%	4.3%	27.9%	23.8%
One	68.2%	95.7%	60.1%	63.6%
Two	16.2%	0.0%	9.6%	9.6%
Three or more	9.8%	0.0%	2.4%	3.0%
All	100.0%	100.0%	100.0%	100.0%

Source: Source ISA coding of Stratified Sample of FWC Agreements also in the Department of Employment Enterprise Agreement dataset. Agreements selected (from many years) were active beyond 31 December 2015.

An analysis of the Department of Employment's data shows that approximately 444,200 employees, or only 4.5 per cent of the workforce[9] have had some form of restriction on their choice of superannuation fund.

The percentage of the workforce with no choice of superannuation fund is only 7.4 per cent which represents 186,000 or 1.9 per cent of all employees.

2.4 Special characteristics of workplaces where limited choice exists

There are unique characteristics applying to those limited number of workplaces where choice of fund to employees is limited which are reflected in the terms of the enterprise agreements to the benefit of employees.

ISA's analysis of the Department of Employment data shows that the limitation of employee choice of superannuation fund found in enterprise agreements is concentrated in certain industries. A total of 17.7% of employees in the private sector covered by agreements have some form of restriction. Table 3 shows the percentage of employees who have restrictions on choice by industry where the percentage is 20 per cent or higher.

Education appears to be the sector where choice is most constrained. This corresponds to significant public sector employment and the unique terms and conditions of superannuation in the higher education sector which utilises UniSuper – the second highest performing fund in the country over 5 and 10 years.

[9] ABS 6333.0 - Characteristics of Employment, Australia, August 2016. Cat. No. 6333.0 which estimates the employed workforce at 9,811,700.

Table 3: Percentage of employees 20% or more where choice is limited by Industry – Private Sector

Industry	Percentage
Agriculture	20
Construction	24
Education	43
Electricity	21
Public Administration	24
Retail	41
Wholesaling	22
Total	**17.7**

2.5 Measures to reduce and mitigate non-payment of superannuation contributions

There appear to be specific industries were the non-payment of superannuation contributions are more prevalent. The naming of specific superannuation funds into which employers must contribute provides a greater capacity for relevant parties, including the superannuation fund, to pursue non-compliant employers.

Industry Funds Credit Control is an organisation utilised by a range of industry superannuation funds for the collection of outstanding employer superannuation contributions. Over the past 5 years IFCC has collected from employers in excess of $618 million in outstanding superannuation contributions.

A key industry in which IFCC operates is the building and construction industry. Insolvency issues and the avoidance of superannuation obligations in the industry are widespread. The timely collection of outstanding superannuation contributions on behalf of employees is much more likely in circumstances where one or a limited number of superannuation funds are listed in enterprise agreements.

Industry Super Australia analysis[10] of tax office data shows that, in 2013-14, almost one in three employees missed out on $5.6 billion in unpaid super entitlements, and, as a result, those nearing retirement had balances that were $23,857 lower on average.

Using conservative assumptions, Industry Super Australia estimates annual superannuation pension drawdowns are $300 million per annum less than they otherwise would be, costing the Government $98 million per annum in extra age pension payments.

ATO data shows that non-payment of superannuation was highest within small to medium sized businesses in the hospitality, construction and cleaning industries.

[10] ISA submission to Senate Economic Committee; Inquiry into Superannuation Guarantee non-payment; ISA Supplementary Submission; March 2017 http://www.industrysuperaustralia.com/publications/reports

Resolving the non-payment of superannuation to employees should be prioritised ahead of changes to enterprise agreement arrangements.

2.6 Payment of additional superannuation contributions

In February 2016 nearly 1.3 million Australians were employed in the retail sector of the economy.[11]

The sector in dominated by young, female and part-time and casual employees.

There is no statutory obligation on employers to make a superannuation contribution on behalf of employees who are under 18 that are employed less than 30 hours per week. This is the case even if those employees exceed the $450 minimum earnings threshold.

Consequently, in the absence of an overriding enterprise agreement, hundreds of thousands of Australians in the retail sector are ineligible for superannuation contributions. Low paid employees in the retail sector have less capacity to privately save for their retirement and are disproportionately disadvantaged by the current limitations applying to superannuation contribution eligibility.

Enterprise agreements in the retail sector have recognised the unique circumstances impacting retail workers and in many instances have required employers to make superannuation contributions on behalf of employees who would otherwise not be eligible to receive contributions. These arrangements have allowed hundreds of thousands of Australians to commence their retirement savings many years earlier than would have otherwise been possible. Whilst these agreements do not always or necessarily provide for choice, this has reduced the administrative burden for employers – particularly relevant in respect of the labour force in this sector of the economy – in connection with providing superannuation contributions that are not otherwise required.

Importantly, these superannuation contributions have been into funds with high long term average performance and relatively low average costs.

The combined impact is that vulnerable retail workers receive a considerable benefit that would otherwise not be available to them.

It is estimated that an employee covered by an enterprise agreement that provides for superannuation contributions to be made from the age of 15 to 18 that would not otherwise be made, will on average receive an additional $6,274 in superannuation contributions at retirement should they remain in the industry super fund. In comparison a retail worker who does not have these additional benefits provided under an enterprise agreement who chooses a bank owned superannuation fund would be a staggering $224,028 worse off in retirement.

[11] ABS Labour force; February 2016 Cat. No 6202.0

Table 4: Estimated $ benefit to retirement incomes of additional EBA provided superannuation contributions ages 15-18

Cameo	Balance at Age 66	Difference
REST EBA covered member age 15 to 66, 8.1% ROR age 15 to 17, 5.4% ROR ages 18 to 66	$845,852	$0
Alt 1: REST no EBA NIL Contributions 15 to 17, 5.4% ROR ages 18 to 66	$839,578	$6,274
Alt 2: Retail fund no EBA NIL contributions 15 to 17, 3.6% ROR ages 18 to 66	$621,823	$224,028

Assumptions: REST rate of return for the 3 years age 15-17 = 8.1% (REST Five Year ROR ending June 2016); Industry fund ROR age 18 to 66=5.4% (10 year APRA industry fund return to June 2016); Retail fund ROR age 18 to 66=3.6% (10 year APRA industry fund return to June 2016); Retail worker average OTE in 2016=$650 pw (ABS Earnings and Hours publication); Full time dependent policy specifications (including LISTO) and IGR consistent economic parameters.

Later in these submissions we make relevant comments regarding the propensity for and capacity of young workers and others to make informed financial choices.[12] Employers and employees in the retail sector of the economy have reached sensible arrangements which, whilst limiting choice of fund, have provided a significant benefit to the relevant employees.

2.7 Insurance arrangements

The inclusion of specific named funds within enterprise agreements in certain industries may be driven by important considerations relating to the provision of automatic group insurance to members of the fund. The insurance arrangements are designed to reflect the insurance needs of the relevant cohort of employees covered by the enterprise agreement and the collective risk profile.

In the health industry, unique and innovative income protection arrangements are designed to provide insurance protection for all workers but relevantly women on parental or other long-term leave.

In the construction industry it is only possible to insurance high-risk occupations via group insurance provided through enterprise agreements. In the absence of agreements which specify named funds and their associated insurance offer, insurance would not be available or affordable for tens of thousands of Australian workers.

The provision of relevant and affordable insurance coverage is an example where the collective provision of group insurance to all employees within a workplace can provide a clear benefit. For many employees, particularly those employed in high-risk industries, the only insurance coverage they will be able to obtain

[12] We note that at various points in the Bill's Explanatory Memorandum it is assumed that when presented with choice of fund only 15 per cent of employees will exercise choice, including the retail industry at paragraph 1.105.

is that provided through their superannuation fund. Consequently, the naming of the relevant fund in an enterprise agreement has been a relevant and material factor in the negotiations between employers and employees at a workplace level.

2.8 Funds named in EBAs have provided superior member outcomes.

Superannuation funds named in enterprise agreements charge members less and deliver on average significantly higher returns. The existing arrangements have provided superior outcomes for members. Most default funds named are not-for profit funds which have over the long-term provided superior outcomes for members.

Table 5: Comparison of 10 year Net Returns from Retail and Not-For-Profit Funds with a Simple 70/30 Portfolio

	10 yr net returns %	Std Deviation
Retail funds	3.50	9.2
Not-for-profit funds	5.30	8.9

Source: ISA analysis of APRA data for 10 years ending May 2017.

Table 6: Comparison of Industry and Retail Fund Expenses per Member, selected years 2004-16

	2004	2007	2010	2013	2016
Industry ($)	74	119	147	210	273
Retail ($)	165	249	246	333	440

Source: ISA analysis of APRA data. Notes: Data is for estimates of fund expenses per member.

The performance differential between bank-owned retail funds and not-for-profit funds is significant. If employees are to exercise choice, they should do so in the context of a level playing field that readily allows consumers to exercise informed choices. It would be a poor policy outcome if those employees that exercise choice switched to an underperforming retail fund.

3. Safeguarding member outcomes

The Bill's Explanatory Memorandum states that the general principle being applied is that "individuals should be able to make decisions about their superannuation that suit their needs."[13]

It is agreed that in a perfect world informed consumers would make rational and informed decisions that suit their needs. The difficulty facing policy makers is that most members of superannuation funds of not exercise choice and when they do, it is generally not informed and consequently there are barriers to rational decisions. The Bill's Explanatory Memorandum estimates that only 15 per cent of employees when offered choice of superannuation fund to exercise choice.

When recognising that most superannuation fund members do not exercise choice the Productivity Commission found that:

> "The failure of many employees to make an active choice is the primary rationale for having a default superannuation system."[14]

3.1 Retirement decisions are complex

There are a range of accepted reasons why retirement decision making is difficult for most employees. These include:

- Lack of financial literacy;
- Complexity of decision making;
- High search costs;
- The 'endowment effect' where people place more value on money lost;
- Lack of price awareness;
- Information asymmetries;
- A long-lag between initial investment and benefit payment;
- An associated tendency toward procrastination;
- Framing effects, where people choose based on how options are framed rather than what is in their best interests.

3.2 Low levels of financial literacy in Australia

With continuing low levels of financial literacy in Australia,[15] the propensity of consumers to make complex financial decisions is not likely to improve in the near future. It is therefore not surprising that a considerable number, in the order of two thirds of fund members, rely on default arrangements in enterprise agreements and modern awards.

The Australian Financial Attitudes and Behaviour Tracker report Wave 4[16] found that 30 per cent of surveyed Australians find dealing with money stressful and overwhelming. This indicates no improvement

[13] Treasury Laws Amendment (Improving Accountability and Member Outcomes in Superannuation Measurers No. 2) Bill 2017 Explanatory Memorandum paragraph 1.61

[14] Productivity Commission Report No. 60 page 3

[15] Australian Financial Attitudes and Behaviour Tracker Key findings report: Wave 4 - Sept 2015 to Feb 2016

[16] ASIC – EY Sweeny, ASIC Report 481: Australian Financial Attitudes and Behaviour Tracker, Wave 4: September 2015-Febuary 2016, Key Findings. (Research undertaken by EY Sweeny on behalf of ASIC which is framed around the five indicative behaviours of

since the inception of the survey. Further, the survey has found a decline[17] in the number of people who said they spend a lot of time thinking about financial information before the making of a decision.

The survey also found that under 35 year olds are more likely to indicate that they have difficulty understanding financial matters. Relevantly for these considerations, the survey reports that only one in three Australians have ever heard of and understood the concept of risk/return trade-off, and that only two in five Australians have ever heard of the concept of diversification.

Admitted levels of financial literacy in Australia are low; particularly amongst certain cohorts, including the young and low income earners. Estimates of financial literacy based on answers to basic financial questions are arguably considerably lower.[18]

When exercising choice and choosing a superannuation fund basic concepts of risk and return trade-offs and diversification are required. The evidence is clear that far too many Australians do not have the required levels of financial literacy to choose a superannuation fund that is in their best interests. Even sophisticated investors often make serious errors.[19]

The work of Delpachitra and Schumann[20] suggests members of superannuation funds see themselves as consumers not investors and lack the ability or time to monitor investments.

Financial literacy surveys[21] demonstrate that financial literacy levels in Australia are low and not improving. The evidence is that far too many Australians are overwhelmed by financial decision making and ultimately do not actively choose. There is no social or economic good to be derived by forcing people to choose. The focus should be on addressing the underlying issues which impact on low engagement whilst simultaneously ensuring there are adequate protections for those that choose and those who do not.

Australia's financial literacy issues are particularly acute for those under 35 years. Any proposal to focus fund choice at the point where an employee first enters the job market will have a distorting impact on the superannuation market. Decisions in the best interests of new employees are long-term decisions. Thoughts of retirement incomes are not likely to be the drivers of decision making at this point. Nor are there any price signals that can be relied on that will be an indicator of likely long-term net returns.

financial literacy identified in the 2011 ANZ Survey of Adult Financial Literacy in Australia and the 2014 Financial Literacy Strategy led and coordinated by ASIC.)

[17] 57% in 2014 to 52% in 2016

[18] Agnew, Julie R.; Bateman, Hazel; and Thorp, Susan (2013) "Financial Literacy and Retirement Planning in Australia," Numeracy: Vol. 6: Iss. 2, Article 7. Available at http://scholarcommons.usf.edu/numeracy/vol6/iss2/art7; also see the work of Iyengar, S. S, and Lepper, M. R, 'When Choice is Demotivating: Can one Desire too Much of a Good Thing?', Journal of Personality and Social Psychology, 79(6), 995, 2000 and Iyengar, S. S., Huberman, G., & Jiang, W, How Much Choice is too Much? Contributions to 401 (k) retirement plans. Pension design and structure: New lessons from behavioral finance, p 83–95

[19] See, e.g., Tversky, A., and Kahneman, D, Judgment Under Uncertainty: Heuristics and Biases, Cambridge University Press, Cambridge UK, 1991 (finding optimism bias in estimating knowledge certainty common to both sophisticated and naïve subjects); Tversky, A. 'Assessing Uncertainty', Journal of the Royal Statistical Society, (finding professional researchers demonstrated erroneous belief in the law of small numbers)

[20] Delpachitra, Sarath and Rafizadeh, Schumann, *The Switching Decision: Are Members of Superannuation Funds Rational and Informed Investors?,* Australasian Accounting, Business and Finance Journal, 8(4), 2014, 45-62. Available at:http://ro.uow.edu.au/aabfj/vol8/iss4/4

[21] Opcit: Australian Financial Attitudes and Behaviour Tracker

The ABS's Adult Literacy and Life Skills Survey in 2006[22] found serious literacy and numeracy problems throughout Australia. Functional literacy levels were found to be at alarmingly low levels in areas with lower socio economic performance indicators such as education, income and employment.

In their recent article *Competition as a means to an end: supply chains and human services*[23] Nicholas Gruen and Chris Vanstone discuss the difficulties of information asymmetry and the beneficial role regulation can play to assist consumer decision making.

"Asymmetric information between different players in the market – buyers, sellers and intended beneficiaries of services – corrupts the generation and flow of information about product quality and the various needs and circumstances of the players."

The 2014 ANZ Survey of Adult Financial Literacy in Australia found a decrease in key financial literacy indicators which indicated a lack of financial sophistication and that this was more prominent amongst under 40 year olds. The survey also found a 'striking' increase in the use of online banking and related financial platforms, particularly amongst younger cohorts.[24]

It is not surprising that a 16 year old with no investment experience, and perhaps little interest, in long-term net returns, will choose personal convenience and immediate benefits. The long-term cost of inappropriate choices will be borne not only by the individual, but all taxpayers.

3.3 Navigating 'Choice'

In superannuation, amid an environment of unstructured choice and hyperactive retailing, individuals must make a series of complex decisions which significantly affect their retirement outcome.

It is evident most people don't choose nor want to choose. In Australia and other countries, member switching in investment choice in superannuation/pension funds currently is relatively low.[25] A study of member behaviour during a 30 month period including the intense volatility of the GFC found that 5 to 6.5 per cent of members made an investment change.[26]

For the small proportion who do wish to choose or are subject to sales efforts to choose better consumer safeguards are strongly warranted.

Consumers are often overloaded with choice with most not possessing the required skills to understand their financial needs; compare literally hundreds of investment options then match their preferences with the optimal product. Expanding choices often reduces engagement rather than increasing it.[27]

[22] ABS: Adult Literacy and Life Skills Survey 4228.0 2006 (reissued Jan 2008)

[23] p://www.themandarin.com.au/author/gruen_vanstone/

[24] *ANZ Survey of Adult Financial Literacy in Australia (2014) The Social Research Centre* (Full report of the results from the 2014 ANZ survey); May 2015

[25] See Agnew et al (2003) Portfolio choice and trading in a large 401(k) plan; Clark-Murphy et al (2008) Retirement Savings Investment Strategy: Member Choices and Performance; Ameriks and Zeldes (2004) How do household portfolio shares vary with age?

[26] Gerrans (2010) (Analysis conducted using data from 4 industry funds and one public sector fund that represent 3.6 million members with superannuation assets (at the time) of $74 billon)

[27] Fear. J, and Pace, G, Choosing not to Choose: Making superannuation work by default and Productivity Commission Inquiry, Default Superannuation Funds in Modern Awards, 2012

Consumers choose based on how available options relate to one another, how they are explained and what other information is provided at the same time - not necessarily which option is in their best interests. Product providers typically shape the frame through which consumer choices are made.

The difficulties associated with choice have led policy makers to develop responses that focus on more intervention to structure or constrain choice. It is important that structured choices are presented to individuals in a manner designed to facilitate careful decision-making that is in their best interests.

4. Requirements for informed choice

To the extent that those employees currently the subject of enterprise agreements will as a result of the proposed changes, be in a position to choose a new superannuation fund, they currently have no reliable measure to compare fund performance and costs and make an informed choice. Informed choice requires ready comparison between funds.

It is suggested by the Government that the changes proposed in the Bill "… will ensure that Australians are able to better understand and compare the performance of superannuation funds across the industry, to see where their funds are invested and have greater ability to switch funds, if they choose to do so."[28]

4.1 Choice must be informed

Behavioural finance shows us that consumers can often make what appear to be irrational or ill-informed financial decisions and that the tendency to do so is greater the more complex or long-term the available choices are. Behavioural finance provides a compelling case for regulatory protections for consumers in the superannuation market.

Professor Cass R. Sunstein[29] of the Harvard Law School suggests that choice can be an extraordinary benefit or an immense burden. Sunstein suggests that in some contexts, people choose not to choose decisions regarding health or retirement plans. Or are prepared to delegate those choices to a private or public institution that they trust (and may well be willing to pay a considerable amount for such delegations).

Sunstein submits that the ultimate judgment in favour of active choosing, or in favour of choosing not to choose, depends largely on the costs of decisions and the costs of errors.

In the context of a publically funded retirement incomes system where the cost of poor or inappropriate decisions is borne by both the individual and taxpayers, the cost of errors can be considerable. Sunstein suggests that directing consumers into appropriate choices has a role to play in avoiding inappropriate decisions.[30]

[28] Minister's Media Release 10 December 2016

[29] Sunstein, Cass R., *Choosing Not to Choose* (February 10, 2014). Harvard Public Law Working Paper No. 14-07. Available at SSRN: http://ssrn.com/abstract=2377364 or http://dx.doi.org/10.2139/ssrn.2377364 Also see *Choosing Not to Choose: Understanding the value of choice*; Oxford University Press, May 2015

[30] ibid Page 11.

In his paper *'If the retail energy market is competitive then is Lara Bingle a Russian cosmonaut?'*;[31] Dr Ron Ben-David, Chairperson Essential Services Commission questioned the effectiveness of competition in the Victorian energy market.

As with the superannuation market, there is a high level of consumer disengagement in the market. Despite large scale marketing campaigns encouraging consumer comparisons and switching, only 13% of customers exercise choice. [32] Complex financial decisions are required to differentiate between the pricing alternatives offered by the various providers. Low levels of financial literacy combined with inadequate information and search costs result in low active choice levels.

It is suggested that there are two primary reasons for this consumer inertia. The first is that all consumers will be receiving the same product, electrons and gas molecules and the second, that the product provided is, as Dr Ben-David suggests, a complex financial product that does not lend its self especially well to active informed consumer choice. It is suggested that there are parallels with the superannuation market, including amongst those the subject of enterprise agreements.

4.2 Different Product disclosure regimes a 'fee-asco'

Consumers are not currently in a position to make an informed choice as there are differing product disclosure regimes for choice and non-choice products. It is currently all but impossible for consumers to compare the fees and costs of the majority of retail superannuation funds with other funds.

ASIC's new Regulatory Guide 97 (or RG97) rules were designed to inject greater transparency into the often opaqueness of indirect investment fees and costs which are unwittingly borne by consumers. However disclosure carve-outs will not enable comparability of costs as retail fund investment platforms are not included. Bank owned retail funds use these platforms to invest the majority of their assets.

This policy decision can result in direct investments in infrastructure and unlisted property looking more expensive, while actually costing the investor less than an investment in the exact same infrastructure or property asset through a listed vehicle or platform. The different disclosure requirements make it almost impossible to achieve consistent and accurate fee and cost disclosure, denying investors the opportunity to accurately compare the products available to them and determine whether a particular product represents value for money.

When making an investment decision consumer watch dogs often warn consumers 'if an offer seems too good to be true, it probably isn't'. Unbelievably, and of course completely inconsistent with reality, many retail superannuation funds when disclosing their investment costs, disclose zero costs. This is of course patently incorrect and misleading, but currently legal.

In such an environment it is difficult to see how a consumer being offered choice can effectively exercise informed choice.

4.3 Choice dashboards

An employee intending to exercise choice of superannuation fund would be forgiven for holding the incorrect view that the same disclosure and information rules would apply to all funds. MySuper products

[31] Dr Ron Ben-David; *If the retail energy market is competitive then is Lara Bingle a Russian cosmonaut?*; presentation to the NEM Future Forum 2015 ,25 June 2015

[32] After adjusting oft stated higher figures to accommodate consumers changing households.

are subject to product dashboard requirements which do not apply to non-choice products. This ensures it is very difficult to compare key product features, including costs and returns. Bank owned retail funds have consistently opposed the introduction of product dashboard requirements.

Simplified Product Dashboards initially commenced in 2013. The timeline below summarises the extraordinary chain of events that has transpired following relentless retail and bank fund lobbying:

- MySuper Product Dashboards took effect from 31 December 2013 with Choice Product Dashboards to commence 6 months later from 1 July 2014;
- Choice Product Dashboards were deferred by an ASIC Class order (CO14/443) until 1 July 2015;
- On 1 May 2015 ASIC further extended the deferral for Choice Product Dashboards to 1 July 2016;
- On 4 May 2016 ASIC further extended the deferral for Choice Product Dashboards to 1 July 2017;
- On 1 June 2017 ASIC further extended the deferral for Choice Product Dashboards to 1 July 2019;
- On 1 June 2017 ASIC also announced, following stakeholder feedback, the Government wished to defer the requirement for employer sub-plans (most of which are offered in the retail sector) to disclose information required under s 29QB in the SIS Act which includes executive officer and director remuneration.

This five year delay to provide simplified disclosure of choice product fees, costs and returns is totally unacceptable and reveals the success of bank owned and other retail funds to create and exploit regulatory differences to suit their commercial objectives and in the course harm consumers.

During the last Parliament the Government sought to amend the Choice Product Disclosure requirements in S 1017BA to water down choice disclosure to just the ten largest investment options despite most bank owned retail funds offering hundreds and in some cases thousands of options. This Bill lapsed with the last Parliament and has not been re-introduced. Plainly retail funds are content with the seemingly endless deferral to escape any simplified product disclosure altogether.

A casual perusal of the net return and cost figures in Tables 4 and 5 are possibility one key reason for the reluctance to encourage comparability across the industry.

The policy priority should be the establishment of a level playing field that enables a consumer to readily compare superannuation products to enable a more informed decision.

4.4 Different regulatory approach to choice and non-choice products

The Government needs to level the choice and non-choice product playing field before interfering with existing arrangements. Employees when exercising choice, should have confidence that the same regulatory regime applies to all available superannuation funds to ensure full transparency across the sector providing comparability and aiding informed choice.

The Government has embarked on an uneven superannuation reform agenda which perversely will result in enhanced scrutiny and regulatory burden on the higher performing and most transparent sections of the superannuation industry whilst disregarding member outcomes in the poorest performing parts of the industry administered by bank owned superannuation funds.

The uneven approach is reflected in the proposed changes to superannuation outcomes tests and assessment framework. The vast majority (83 percent) of bank-owned and other retail superannuation assets are held outside MySuper and will be excluded from the new enhanced obligations. This is the case notwithstanding that the excluded products on average underperform MySuper products. New powers provided to APRA, including enhanced directions powers; look through reporting requirements and the power to revoke licenses will not apply to bank-owned and other vertically integrated retail superannuation funds.

At a minimum the Parliament should insist that comprehensive and consumer friendly Choice product disclosure and outcome tests are delivered before agreeing to any broadening of choice of fund provisions.

Attachment 1 – Rice Warner Report (Member Switching)

RICEWARNER
Insight like no other

Member Switching

Industry Super Australia

12 September 2017

SYDNEY
Level 1
2 Martin Place
Sydney NSW 2000
P +61 2 9293 3700
F +61 2 9233 5847

MELBOURNE
Level 20
303 Collins Street
Melbourne VIC 3000
P +61 3 8621 4100
F +61 3 8621 4111

ABN 35 003 186 883
AFSL 239 191

www.ricewarner.com

Table of Contents

1. Executive summary 2

1.1 Overview 2

1.2 The Data 2

1.3 Summary of findings 2

2. Background 5

2.1 Introduction 5

2.2 The dataset 5

3. Member rollovers 8

3.1 Summary of APRA statistics 8

3.2 Demographic trends in member flows 12

3.3 Are members' switches based on fund outcomes?.... 18

3.4 Cumulative rate of exit 28

This report constitutes a Statement of Advice as defined under the Financial Services Reform Act. It is provided by Rice Warner Pty Ltd. which holds Australian Financial Services Licence number 239 191. This report should not be distributed, in whole or in part, without Rice Warner's prior written consent.

1. Executive summary

1.1 Overview

This report has been commissioned by Industry Super Australia (ISA) to assist it in responding to the Productivity Commission's (PC) three stage review into the efficiency of the Australian Superannuation system. The purpose of this report is to examine switching trends of superannuation members. We examine whether switching activity is consistent with members making informed decisions which will improve their retirement outcomes.

In this report, we examine trends in member rollover and switching behaviour both in relation to the number of members and the size of benefits (assets) transferred. Specifically, we address:

- Demographic trends in member rollover and switching behaviour.
- Whether member switches provide improved outcomes, namely:
  - lower fees following the change
  - improving the likelihood of improved investment returns based on historical investment performance (net returns).
- Switching rates from employer sub-plans to personal superannuation.
- Cumulative probability of member exit over three years.

1.2 The Data

In this report, we utilise data published by APRA supplemented by Rice Warner's own *Superannuation Insights* study, which involves the collection of annual statement data pertaining to over 10 million members per annum. Further information on the dataset can be found in Section 2.2 (The dataset).

1.3 Summary of findings

From this research, we have been able to make several observations for the sample based on data from 2013 to 2015.

1.3.1 Aggregate rollovers and switches

Based on both the Superannuation Insights sample and APRA statistics, retail funds have been the largest beneficiary of rollover activity, relative to switches to industry, corporate and public sector funds. APRA statistics show 72% of rollovers have a destination in the retail sector (at June 2015):

Retail:	$44.7b	72.1%
Industry:	$12.5b	20.2%
Public Sector:	$3.8b	6.1%
Corporate:	$1.0b	1.6%
Total:	**$62.0b**	**100.0%**

1.3.2 General findings about switching behaviour

We have observed the following demographic trends in member switching behaviour:

- A majority of this switching activity is concentrated around age 30, then tails off before peaking again just prior to retirement age. Retail funds are more likely to be the switching destination for members at all ages, in particular for members with balances in excess of $50,000.
- Members with balances over $100,000 are twice as likely to switch to a retail fund relative to an industry fund, though smaller balance accounts are more likely to be subject to a rollover to another fund, regardless of sector.
- Gender differences in rollover activity are generally small. However, it appears that women are less likely to switch funds between ages 30 and 50, which may be the result of taking time out of the workforce and being less engaged with super throughout this period.
- Members with longer tenure in the same fund remain loyal and are less likely to rollover.

1.3.3 Are decisions based on outcomes?

We have observed both fees and historical performance for incumbent and successor funds from member switches.

1.3.3.1 Fee outcomes and switching

When comparing the level of fees before and after a member switch, we observe that:

- Members are unlikely to have used fee levels as a primary reason for switching between funds, as many members are charged a higher fee after switching.
- 20% of members pay lower fees after switching funds, while 49% of members pay higher fees. 31% of members did not have a notable increase or decrease in fees paid (with a margin of $10 either way).
- The aggregate fee outcomes from switching activity reveals a net increase of $137 million in fees. The major component of this is a $170 million increase in fees as a result of switching into funds with higher fees. Retail funds account for 92% of this increase in fees. This is modestly offset by a $33 million saving in fees. For not for profit funds, the impact is not as stark, with an aggregate increase in fees of $13 million, against a decrease of $9 million.
- These outcomes for retail funds are driven by 59% of switching members paying increased fees, at an average increase of $263 per person annually. Compared to industry funds, a similar proportion of members switching pay higher fees (50%), though the average increase for these members is only $83.
- Members rolling into industry funds are generally going to be twice as likely to pay lower fees than those rolling into retail funds (21% against 9%). The average decrease on fees for those paying lower fees is also greater for those rolling into industry ($110 p.a.) rather than retail ($55 p.a.) funds.
- For members switching from industry to retail funds, only 7% paid lower fees at the new fund. Conversely, 78% of members switching from retail to industry funds paid lower fees.

1.3.3.2 Return outcomes and switching

When comparing performance of funds (using a 4 year period to 20 June 2015) before and after a member switch, we observe that:

- Members are unlikely to have used past performance as a proxy for their investment decision as the data shows on average that historical returns for the incumbent and successor fund tend to be similar.
- 36% of members would have received higher returns over the period, while 56% of members would have received lower returns. 8% of members did not see a notable increase or decrease in investment performance (with a margin of 0.05% either way).
- The aggregate estimated impact on investment returns reveals a net decrease of $284 million annually. This Is largely driven by a $373 million decrease in returns annually for members rolling into funds with lower returns. Retail funds accounted for 87% of this decrease in returns. This is offset by an $89 million increase in annual returns for those members switching into higher performing funds. 52% of this increase is accounted for by industry funds, while only 33% is by retail funds.
- These outcomes for retail funds are driven by 80% of members switching into retail funds achieving lower returns, at an average of 0.91%. Conversely, only 36% of members switching into industry funds achieved lower returns, at an average of 0.63%.
- For those rolling into higher performing funds, the average increase was 0.39% for retail funds vs. 0.72% for industry funds. For those rolling into lower performing funds, the average decrease in returns was 0.91% for retail funds vs. 0.63% for industry funds.
- Compared to industry funds, the outcomes for those rolling into retail funds are thus more likely to be negative. Further, the scale of this impact is also estimated to be larger for those rolling into retail funds.

1.3.4 Estimated impact of switching on member outcomes

At an aggregate level, and assuming that fees and performance remains constant, we have estimated that:

- The estimated aggregated net impact of switching funds is an **increase in $137 million p.a**. being paid in fees by members.
- The estimated aggregated net impact of switching funds on investment performance is a **decrease in returns of 0.46%, or $284 million p.a.**

This report was prepared and peer reviewed for Industry Super Australia by the following consultants.

Prepared by	Peer Reviewed by
[redacted]	[redacted]
Nathan Bonarius Consultant	Alun Stevens Senior Consultant
[redacted]	[redacted]

12 September 2017

2. Background

2.1 Introduction

The Productivity Commission (PC) is currently undertaking the third stage of its review into efficiency in the superannuation market. The second stage examined alternative models for the allocation of default business in the superannuation market. This report has been commissioned by Industry Super Australia (ISA) to assist it in responding to the PC review. In it, we examine trends in member rollover and switching behaviour based on activity reported to APRA and a sample of exits in Rice Warner's *Superannuation Insights* study.

The report focuses on member flows in the superannuation system between products (including both default and choice products) split by members and by asset flows. We provide detailed explanation of the most used channels and examine the changes in investment returns and fees that the members would have experienced resulting from their movement between products.

2.2 The dataset

2.2.1 APRA Data

In addition to the Superannuation Insights data we have also examined statistics published by APRA. The APRA data provides a market wide benchmark that complements the depth of the Superannuation Insights data. We have examined the following sources for this report:

- **Annual Fund Level Superannuation Statistics** - this contains detailed profile and structure, financial performance and financial position, conditions of release, fees and membership information for APRA-regulated superannuation funds.
- **Quarterly MySuper Statistics** – this contains data on MySuper products. The report contains information on the product profile, product dashboard measures, asset allocation targets and ranges, investment performance, fees disclosed for MySuper products, or where relevant, for the lifecycle stages underlying MySuper products with a lifecycle investment strategy, and MySuper URLs.
- **Annual Superannuation Bulletin** – this contains statistics that provide policymakers, regulators, trustees and the community with information to assess the overall performance of the superannuation system.
- **Annual MySuper Statistics** – this contains detailed data for all MySuper products, and allows users to analyse APRA-regulated MySuper products across a range of measures.

2.2.2 Superannuation Insights

Superannuation Insights is a yearly data analysis project undertaken by Rice Warner which involves the collection of anonymised details for more than 10 million member accounts per annum. The database is the only one of its kind for superannuation members and supplements our other research in forming the basis for many of our insights into the superannuation market.

The data used to carry out the study is de-identified member data at 30 June in 2015, 2014 and 2013, which includes relevant data for members who exited the fund during the financial year. The data requirements are substantially aligned with the data used for benefit statements at the end of each financial year.

The data used for Superannuation Insights covers the following aspects of the market:

- Demographics
- Investments
- Contributions
- Insurance
- Fees
- Employers
- Pensions
- Exits.

The sample is drawn from a variety of large and small funds that represent all market sectors (industry, retail and some public sector and corporate funds).

This data allows us to provide detailed analysis across several key areas:

- Analysis of membership profile by different segments and comparison with the peer group.
- Quantifying and comparing differences between members across gender, ages and geographic area.
- Understanding inflows of funds from contributions and roll-ins.
- Investment strategy – participation in default strategies versus choice investments, and how choice members differ from default members.
- Insurance analysis – take up of cover and average levels of cover along with analysis of insurance needs.
- Employer analysis – including average number of employers, average employer size, distribution of employers.
- Pensions – demographic and behavioural analysis of pension members including investment decisions, drawdown rates and balance analysis.
- Exits analysis – identification of key areas of member leakage from funds in absolute terms and the dynamics of the exiting membership.

2.2.3 Caveats and limitations

Although the Superannuation Insights data is extremely detailed and represents a significant sample of the superannuation industry, there are the following limitations. Overall, the quality of the sample is determined by the participant funds and despite the large overall participation in the study, there is still a bias in the data we have collected. For instance, the sample is skewed by the largest funds in the study – AustralianSuper has 2 million member accounts of the total 10 million in the sample. Also, members who may currently be in smaller, high cost funds are less likely to be a part of the sample. Lastly, not all funds have provided consistent exit data which can be mapped year on year; some funds have only participated in some of the given years.

Data on fees and investment performance have been drawn separately from Rice Warner's Superannuation Product database.

Limitations on certain data points

- Fees are not known for members exiting to an employer sub-plan superannuation product where they might have received a discount. We have identified these movements separately in the fees analysis and provided our own estimate based on MySuper statistics published by APRA.
- The data sample for corporate funds is relatively small.
- Members with missing investment information (in the incumbent fund) were assumed to be in the default option.
- Investment selection in the successor fund is unknown, we have assumed members select a similar option to the incumbent (based on default status or asset allocation) so that comparisons are on a like-for-like basis.
- When mapping fees on a product level, data limitations meant that a subset of members who rolled over had to be omitted from the analysis.

Not all data was provided by all funds

Although every effort is made to collect all the appropriate member data for Superannuation Insights, some funds were unable to provide complete data sets. Whilst the core areas of Superannuation Insights, such as demographics, insurance and investment, are substantially complete, some funds have not provided all details for exited members, and are omitted from demographic analysis.

Incomplete longitudinal results

Longitudinal analysis requires new participants to provide previous years' data. In some cases, this has been a large administrative burden and the funds have not complied. Funds which have participated in earlier years have had their data automatically analysed longitudinally.

Unable to examine SMSFs

We have not undertaken any analysis of differences in fees or investments for members moving to an SMSF as data is not available.

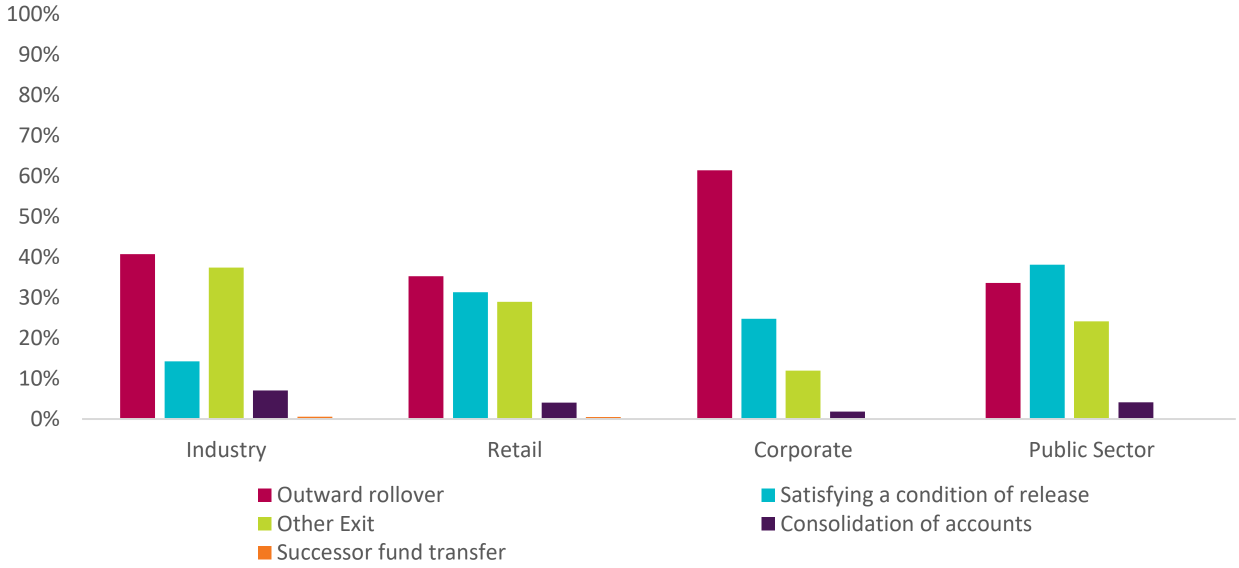
3. Member rollovers

3.1 Summary of APRA statistics

APRA statistics allow us to examine the overall composition of the market.

Graph 1 shows the percentage of member exits by type of exit. When examining the Superannuation Insights data, we focus on 'Outward rollovers' and other types of exit have been excluded.

Graph 1. Percentage of member exits by type - year to June 2016



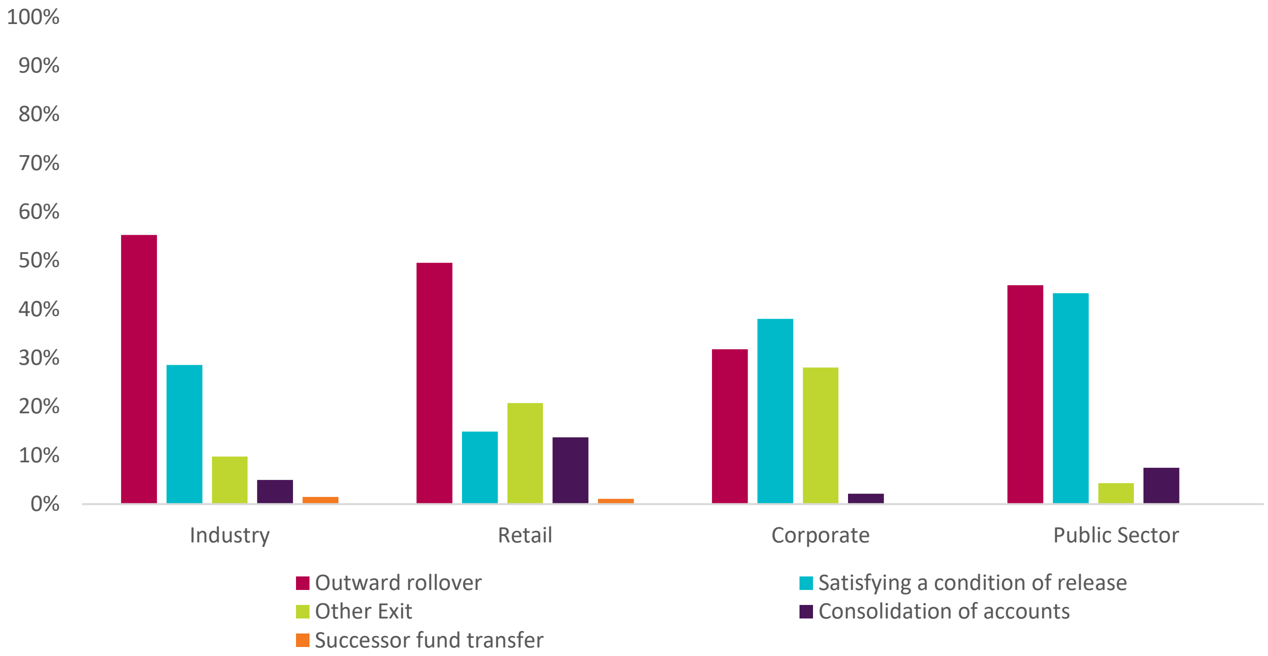
Source: APRA Fund Level Statistics.

Outward rollovers remain the biggest source of member exits across the industry, with the public sector as the exception, this is driven by demographics. Member growth in this segment is low and their population is aging, which explains why most member exits are as a result of satisfying a condition of release, which will primarily be retirement.

Other exits are not clearly defined by APRA in the reporting requirements, but likely include other forms of account closure such as zero balance closures and transfers to the ATO of lost superannuation.

Graph 2 shows the percentage of asset exits by type of exit.

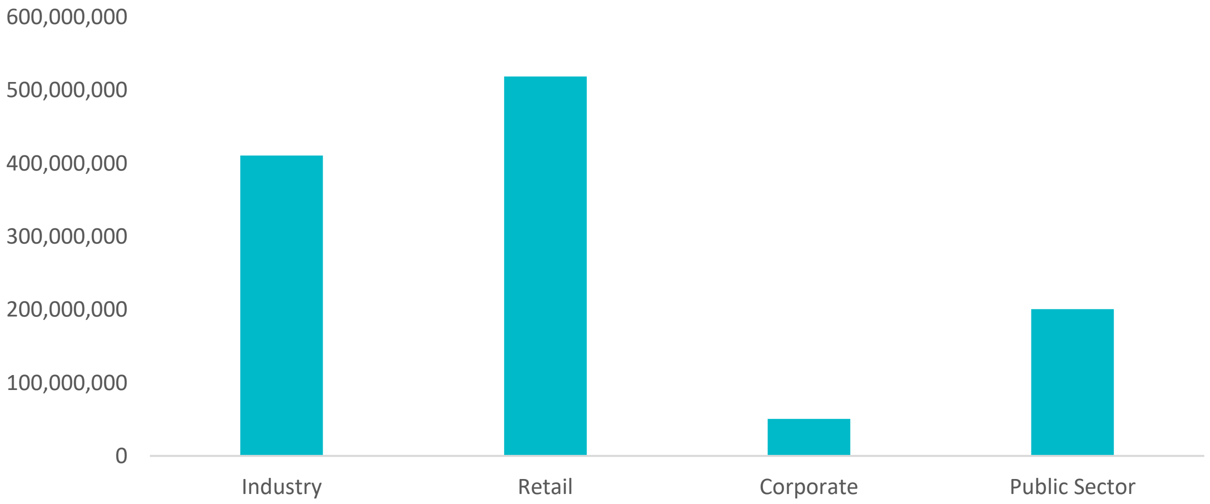
Graph 2. Percentage of asset exits by type - year to June 2016



Source: APRA Fund Level Statistics.

Graph 3 shows the split of total industry assets between the four major APRA regulated sectors.

Graph 3. Total Assets – APRA Regulated Funds ($,000)

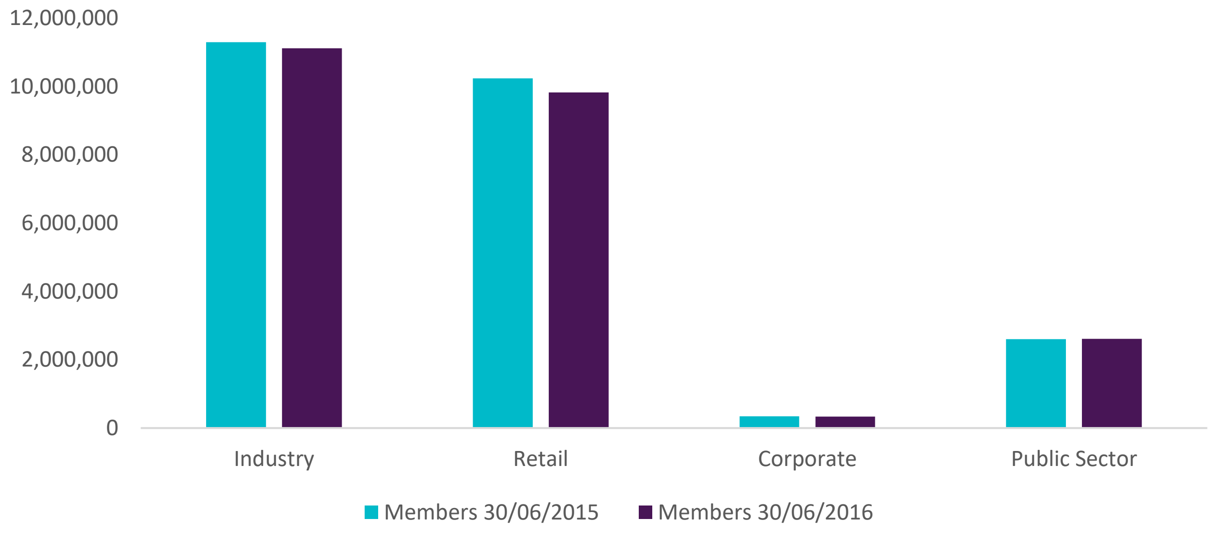


Source: APRA Fund Level Statistics.

Industry and retail funds continue to dominate the landscape, albeit for different reasons. Corporate funds have continued to shrink and now represent less than 5% of assets. Market shares are useful to inform commentary on exits between sectors as larger sectors are likely to attract more rollovers simply due to the number of competitors and size of budgets for marketing and other activities.

Graph 4 shows the total number of member accounts for each sector between 30 June 2015 and 30 June 2016.

Graph 4. Total member accounts (exluding ERFs) 2015 - 2016



Source: APRA Fund Level Statistics.

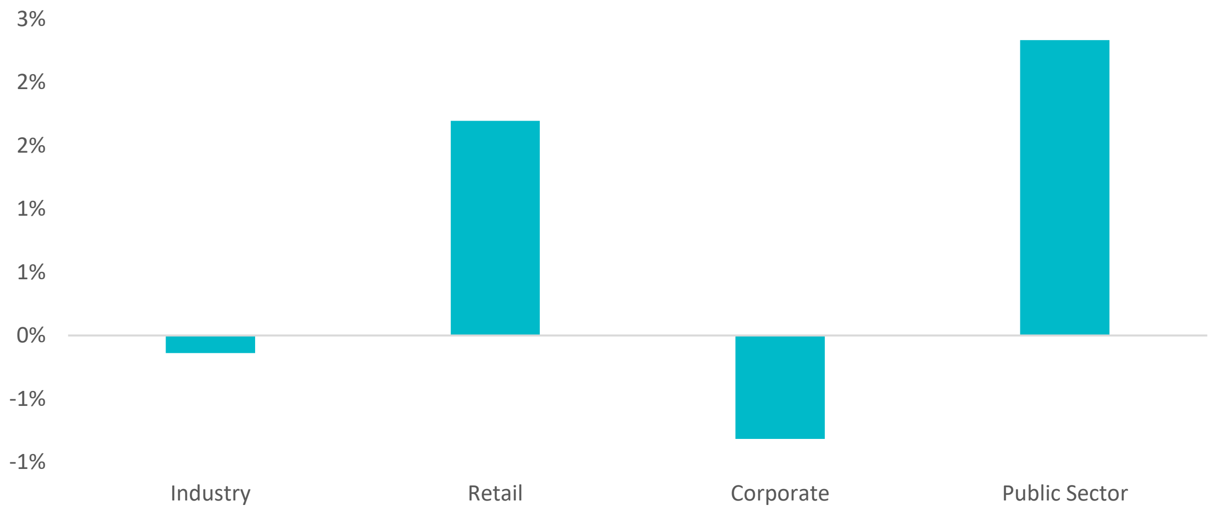
The number of superannuation accounts is falling for two reasons:

- Lost accounts with amounts below $6,000 are now swept into the ATO, which attempts to find members so they can transfer the amounts into their active account.
- All superannuation funds run campaigns to encourage members to consolidate their accounts. Usually, members consolidate all inactive accounts into their current active account.

Over the year, only public sector funds experienced growth in the number of member accounts, but it was only 0.2%. The other three sectors all declined with retail experiencing the greatest reduction of 4.0%.

Graph 5 shows the net rollovers for each sector as a percentage of FUM in FY2016.

Graph 5. Net rollovers – APRA regulated Funds ($'000)



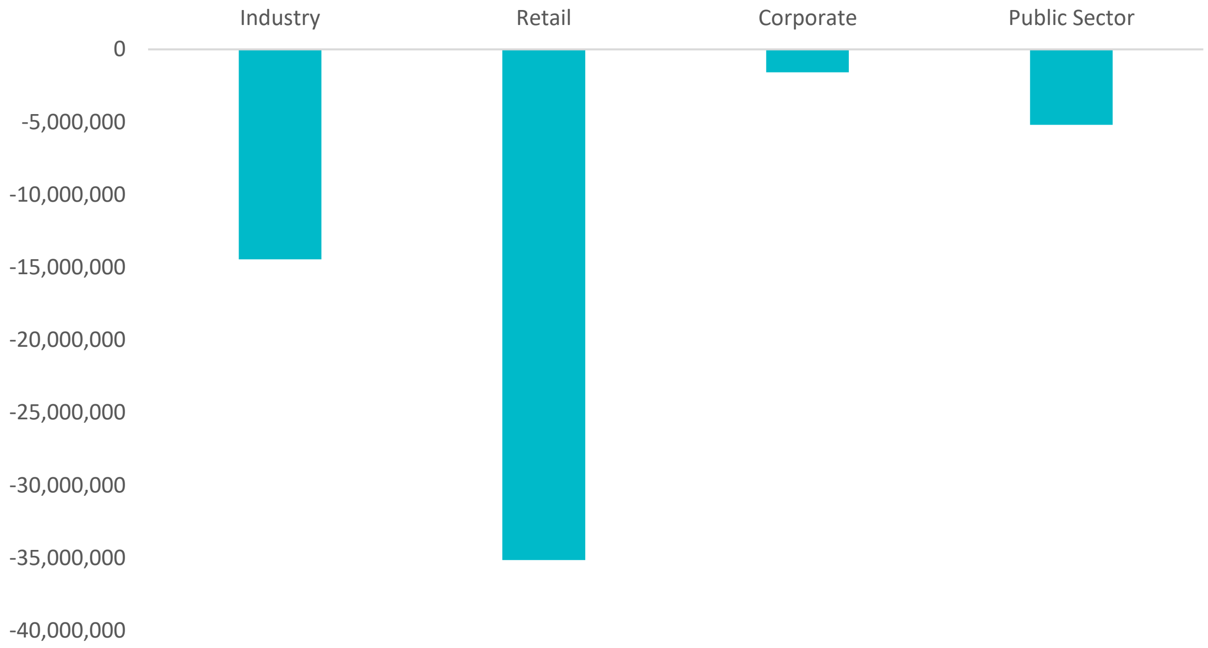
Source: APRA Fund Level Statistics.

Unsurprisingly, corporate funds suffered the largest net rollouts for the year. As unengaged employees change jobs, they will often shift to the fund used by their new employer. As members develop an interest in their superannuation, they are more likely to maintain the same fund even when they change employer. This is less likely to occur if they leave a corporate fund.

Public sector funds had the highest inward net rollovers, with retail close behind. Industry funds experienced a small net outflow overall, largely due to the transfer of inactive accounts to the ATO.

Graph 6 shows the total outward rollovers by sector.

Graph 6. Total outward rollovers



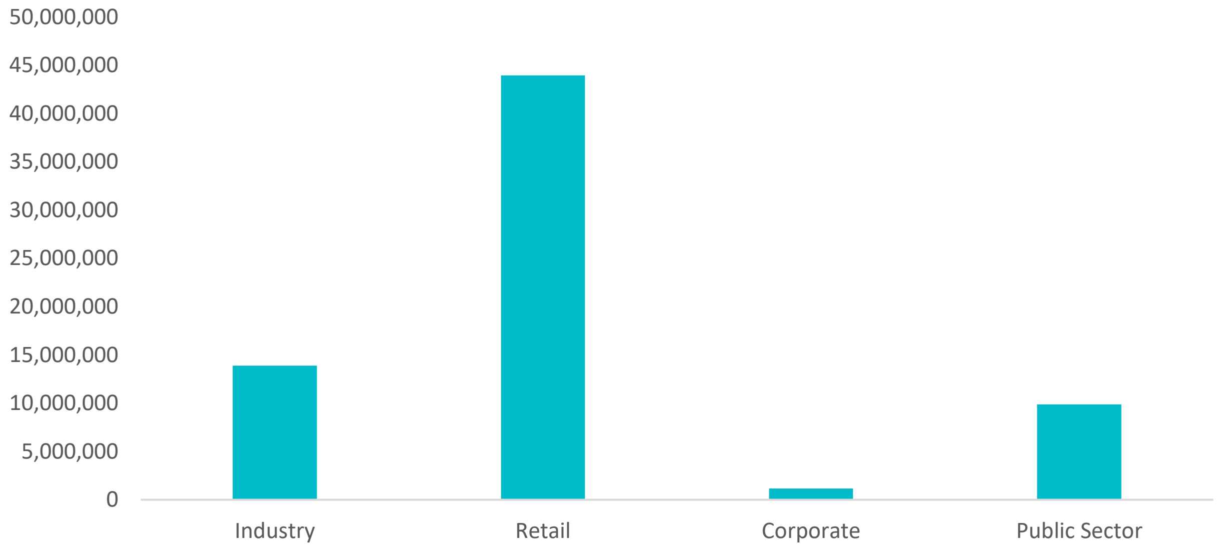
Source: APRA Fund Level Statistics.

Although the retail sector has positive net rollovers, it still has the largest outward rollover flows of the system, and greater than the combined outward rollovers of industry, corporate and public sector funds.

We note that retail funds have a more transactional relationship with their customer base which is driven by higher levels of choice and advice distribution channels. Not for profit funds seek to promote trustee management of investment and distribute products to a greater degree through wholesale channels and therefore may have a larger default membership base that may be less likely to change funds.

Graph 7 shows the total outward rollovers by sector.

Graph 7. Total inward rollovers by sector



Source: APRA Fund Level Statistics.

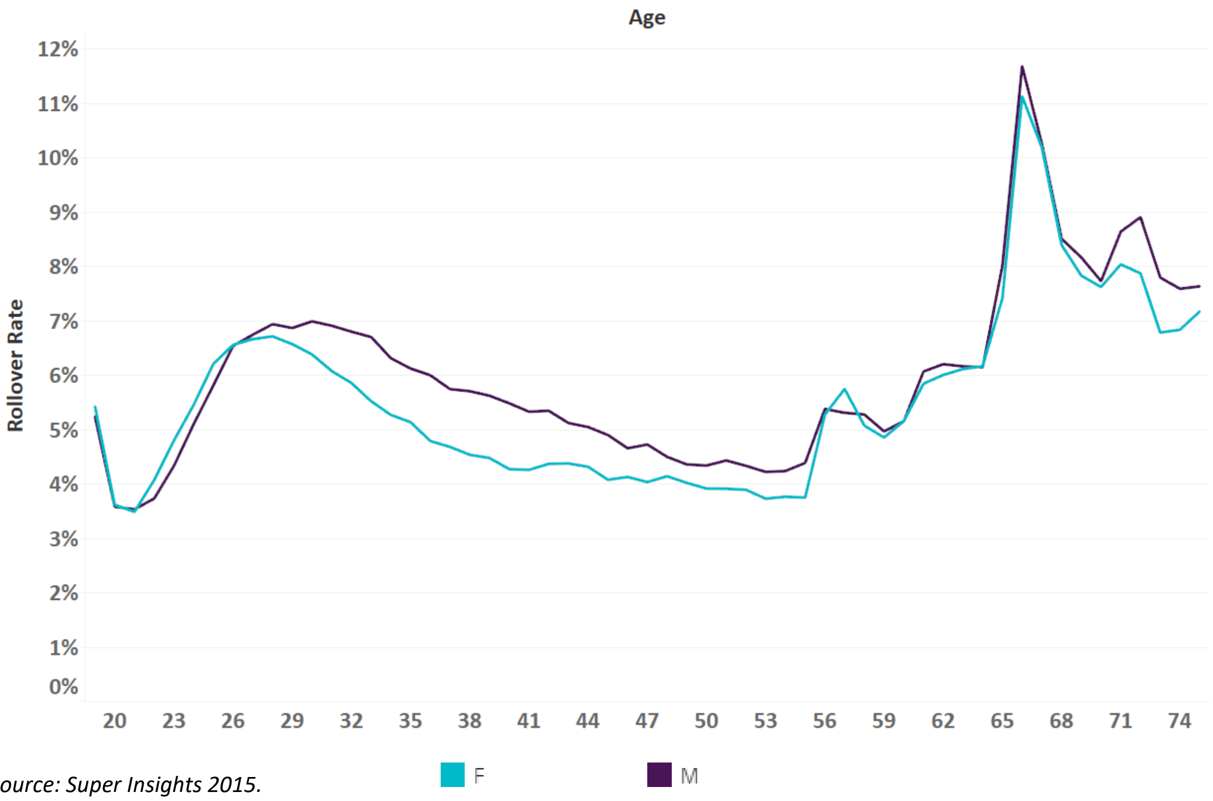
The retail sector has the largest inward rollovers of all the sectors. These are greater than the outflows for the retail sector. There is likely a lot of movement between funds within the retail sector. Corporate funds remain a relatively small part of inward rollovers, unsurprising due to the small size of this sector and the declining number of corporate funds. Public sector funds have much larger inward rollovers than outward, and industry funds have slightly lower inward rollovers than outward.

3.2 Demographic trends in member flows

The APRA data presented above provides context for the remainder of this report which is based on Rice Warner's *Superannuation Insights* exit data.

Graph 8 shows the proportion of members in each age group rolling over by gender.

Graph 8. Proportion of members rolling over by age and gender



Source: Super Insights 2015.

Superannuation members change their superannuation fund more frequently than they would change bank accounts. More than 5% of accounts are changed annually.

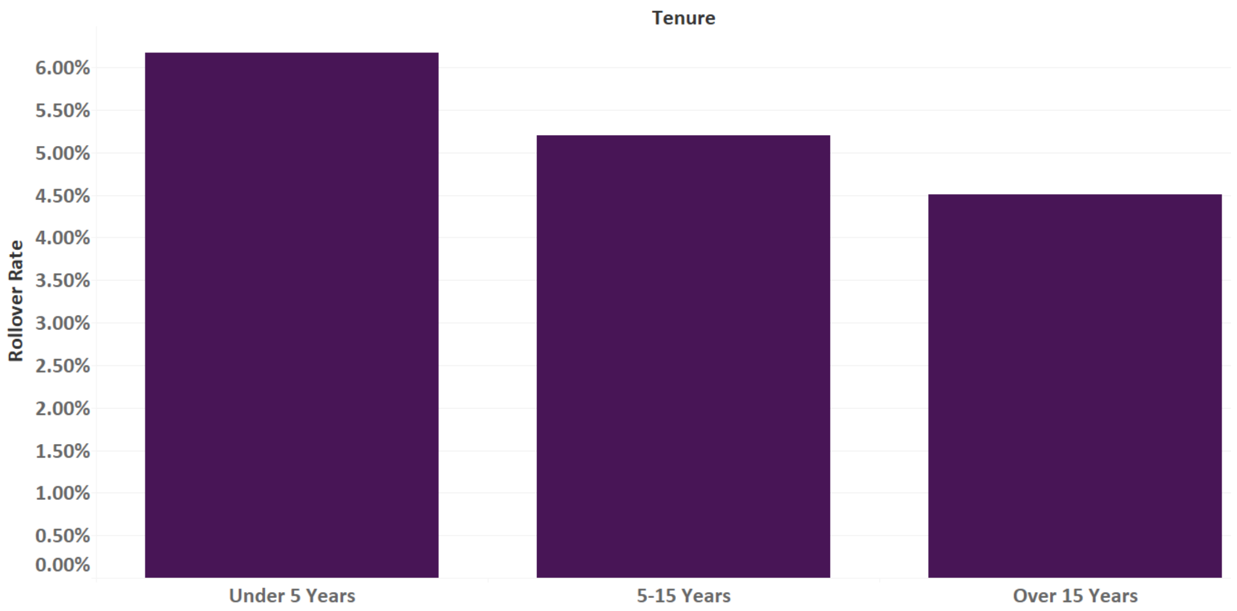
We note that males are more likely to rollover than females and this is consistent across the life-cycle. This is possibly a result of gender differences in workforce participation, rather than a gendered attitude to superannuation. The difference is most pronounced during the 30s where women are more likely to take time out of the workforce to raise children with some mothers never returning to work or waiting until their last children have finished school.

Rollover activity quickly ramps up between the ages of 20 and 30 as members begin to start their careers and move on from earlier jobs. We expect that this is at least partially driven by the movement of members into more stable, long term employment and other factors such as cross selling of products for example, at the point of taking out a mortgage. Male rollover activity continues to increase, peaking around age 30 before trending downwards. Females begin to trend down after approximately age 28. We expect that this is driven largely by lifestyle factors, such as starting a family.

Greater engagement with superannuation from age fifty-five is likely a result of members preparing for retirement (and accumulating larger balances). There is a spike for both females and males at age sixty-five, almost certainly the result of the consolidation of accounts and transfer into retirement products.

Graph 9 shows the proportion of members rolling over segmented by the amount of time they have spent at a fund.

Graph 9. Proportion of members rolling over by tenure at fund

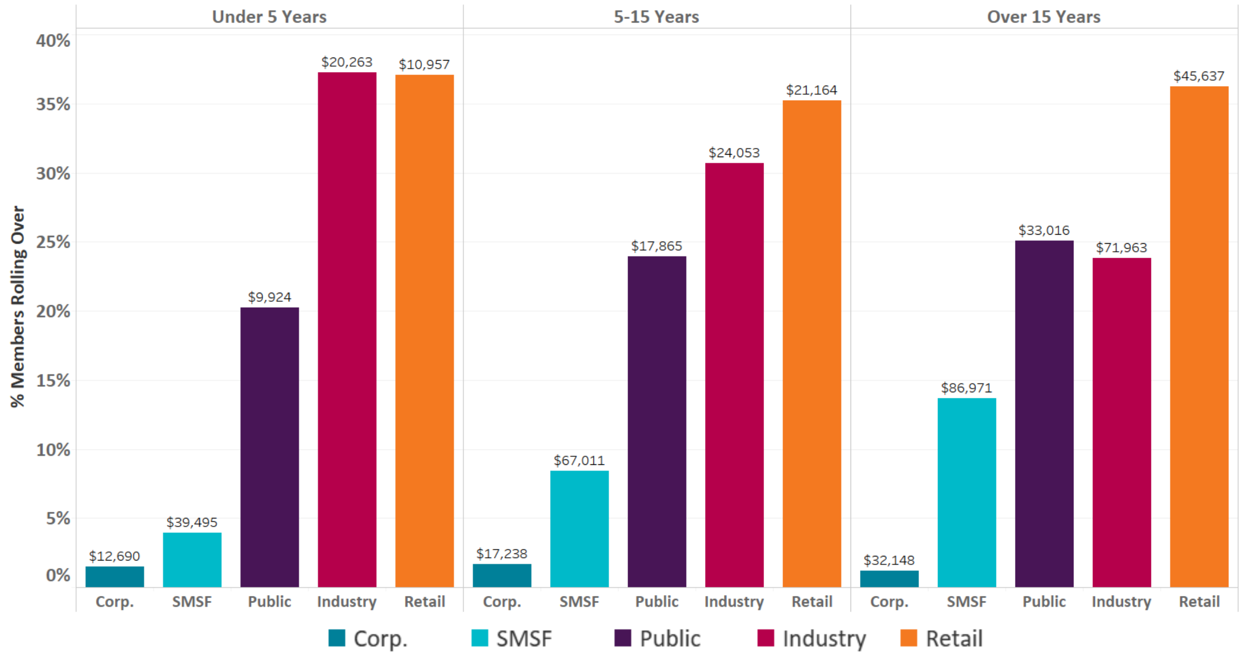


Source: Superannuation Insights 2015.

The rate of exit is negatively correlated with tenure, this is likely the result of survivorship bias. Many members who are comfortable with their fund will stay in it throughout their working life. Those who are unengaged are less likely to transition out of the fund.

Graph 10 shows the destination fund type for members by tenure.

Graph 10. Destination fund of members rolling out and average balance rolled over by tenure



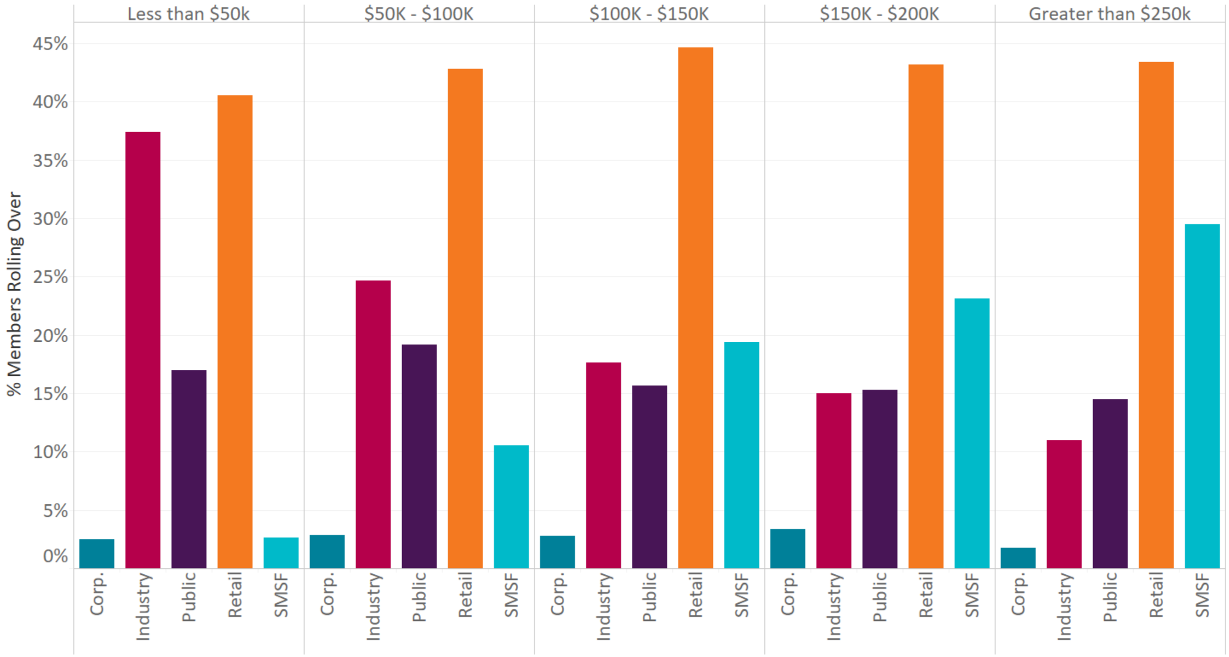
Value labels indicate average balanced rolled over, column height indicates the distribution of accounts by sector.

Source: Superannuation Insights 2015.

The largest balances at all durations go to SMSFs. However, more members go to retail funds. Retail funds maintain their share of member switches at higher tenures c. 35% of all exits, whereas industry funds have a lower share at higher tenures c. 25%. SMSFs and public sector funds have a greater share of rollovers at higher tenures.

Graph 11 shows the destination fund type for members by balance amount.

Graph 11. Destination fund of members rolling out by balance



Source: Superannuation Insights 2015.

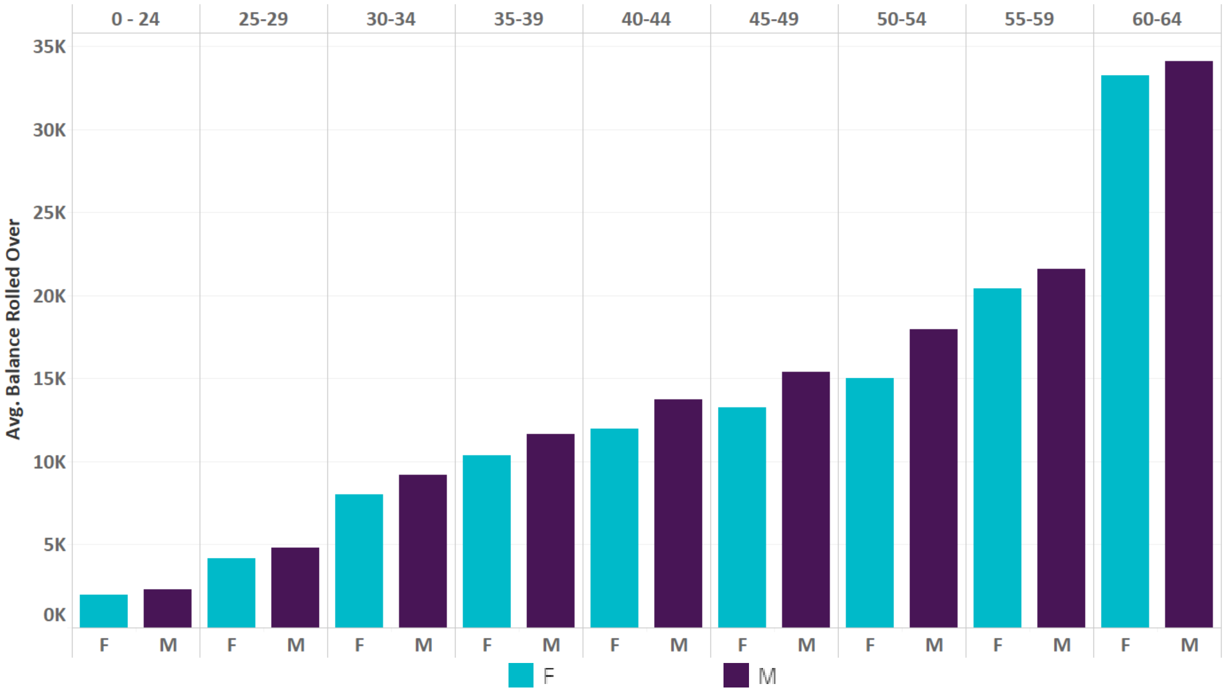
The retail sector has the greatest share of exits at all balances considered in Graph 11. As balance increases the retail sector's share of exits increases initially from 40% (at balances under $50,000) to 45% (for balances over $100,000). The proportion of members rolling into industry funds is highest for balances under $50,000 at around 37% and falls to about 10% for balances of $250,000. The probability of a switch being to a retail fund is roughly double that of industry funds for balances over $100,000.

SMSFs are much more likely to be the source of rollovers for balances over $250,000 where they represent 30% of exits. This makes sense given the large balance required to make an SMSF cost effective.

The rate of rollover to corporate and public sector funds remains relatively constant across balance bands.

Those members with tenure in a single fund above 15 years are also more likely to rollover to SMSFs or retail products (perhaps because of targeted financial advice programs) and are less likely to rollover to industry superannuation funds. Tenure has a clear positive correlation with age and balance, and the longest serving fund members are likely to be much older, partially explaining the bias towards SMSF arrangements.

Graph 12. Average rollover amount by age and gender



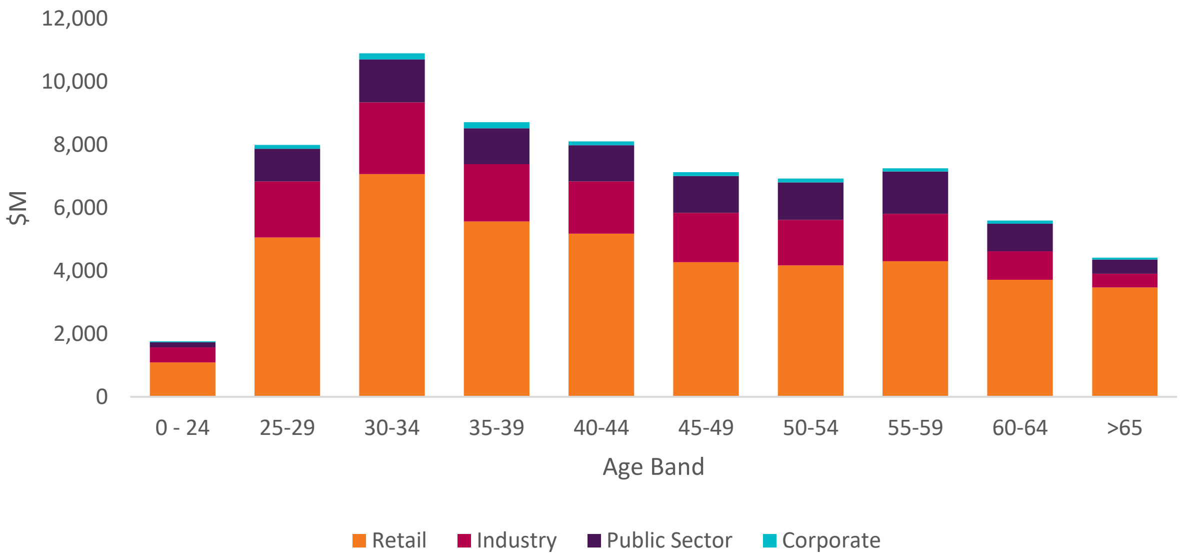
Source: Superannuation Insights 2015.

Overall the amount of money which is rolled out by members increases with age which is unsurprising. What is of interest is that the average rollover amounts are much lower than average account balances, implying that smaller accounts are being consolidated into larger accounts. Of further interest is that the gap between male and female rollover balances is smaller than the general gender gap in account balances. This is most likely a function of small lost inactive accounts being rolled over into the primary accounts and it is these that reflect the gender gap.

Graph 13 shows an estimate of total rollovers into each sector broken down by age, based on a combination of APRA and our own Superannuation Insights statistics. The totals by sector for Graph 13 are:

Retail:	$44.7b
Industry:	$12.5b
Public Sector:	$3.8b
Corporate:	$1.0b
Total:	**$62.0b**

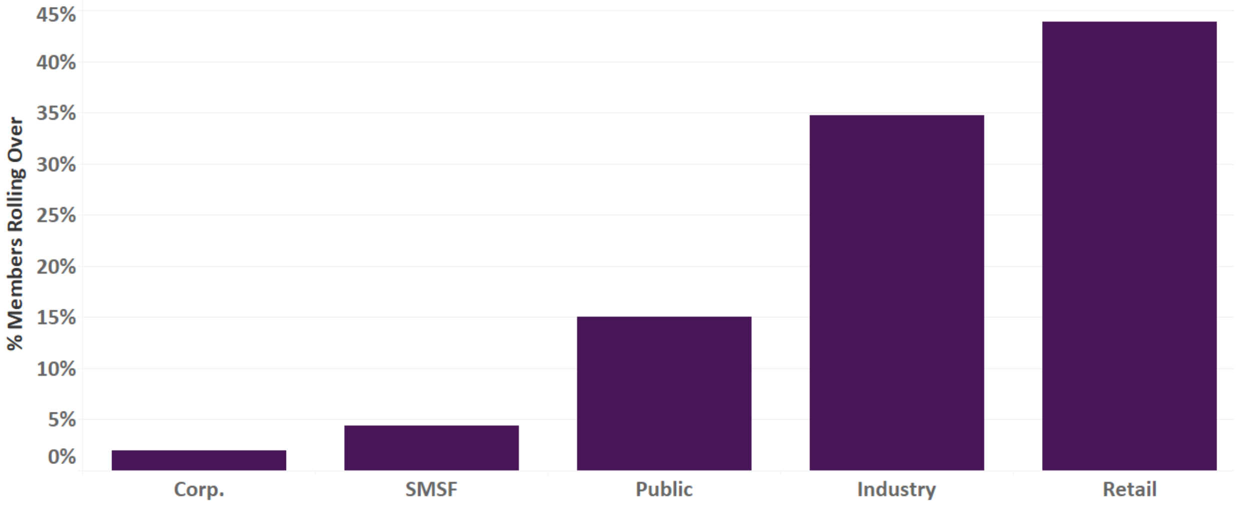
Graph 13. Estimated aggregate rollovers to sector by age by sector (excluding SMSFs) – year to June 2015



Source: Rice Warner estimate using APRA Fund Level Statistics and Superannuation Insights 2015.

The dollar value of rollovers to retail funds dominate at all ages. While the size of rollovers to industry funds remains relatively constant between ages 25 and 60, retail funds take a relatively larger proportion of rollovers above age 60.

Graph 14. Proportion of exits by rollover destination

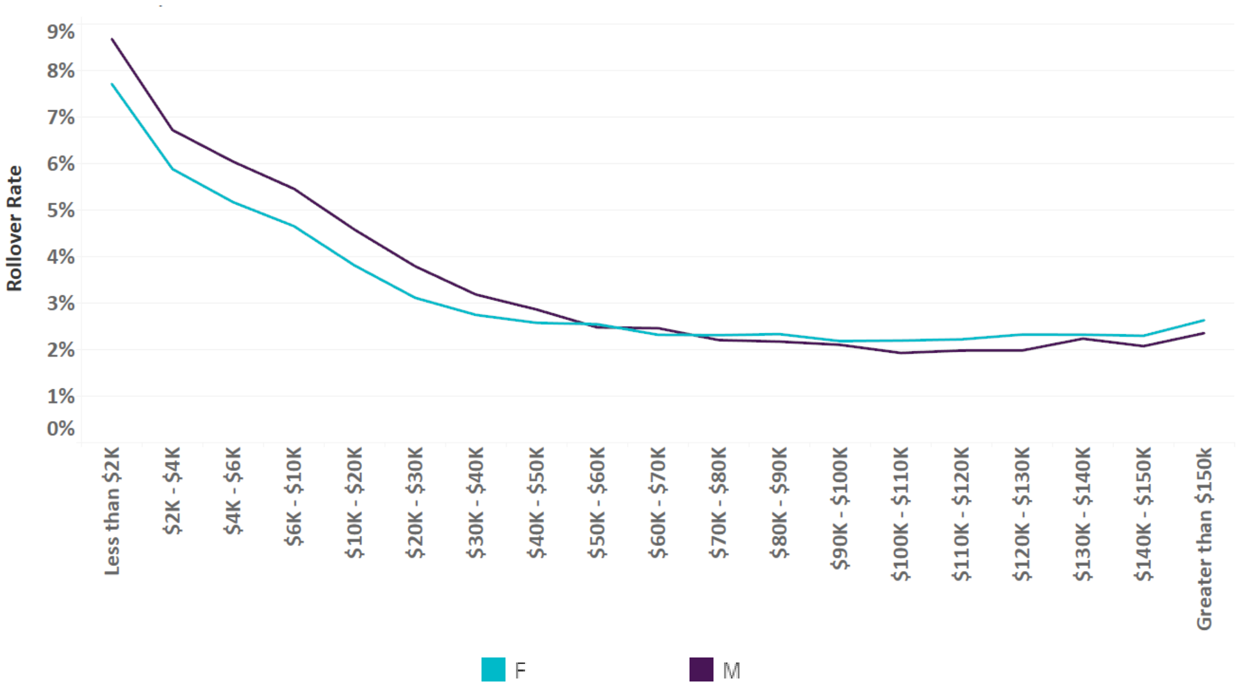


Source: Super Insights 2015.

Our destinations for exited members are consistent with APRA statistics. Retail funds are the primary destination for rollovers. The success of retail funds can be partially attributed to adviser distribution channels, the direct cross selling of superannuation products to customers of everyday banking and mortgage products under *share of wallet* initiatives and participation in the corporate outsourcing (wholesale) market.

Graph 15 shows the percentage of rollovers occurring in each balance band.

Graph 15. Percentage of rollovers by balance band



Source: Superannuation Insights 2015.

Smaller balance accounts generally form the bulk of rollovers. This is a function of consolidation activities of unneeded accounts or transfer of existing balances on a change of occupation.

3.3 Are members' switches based on fund outcomes?

The Productivity Commission is interested in whether members are being appropriately served by the superannuation industry in current default market structures. Member outcomes form the basis of the Commission's analysis into whether the superannuation market is efficient and competitive.

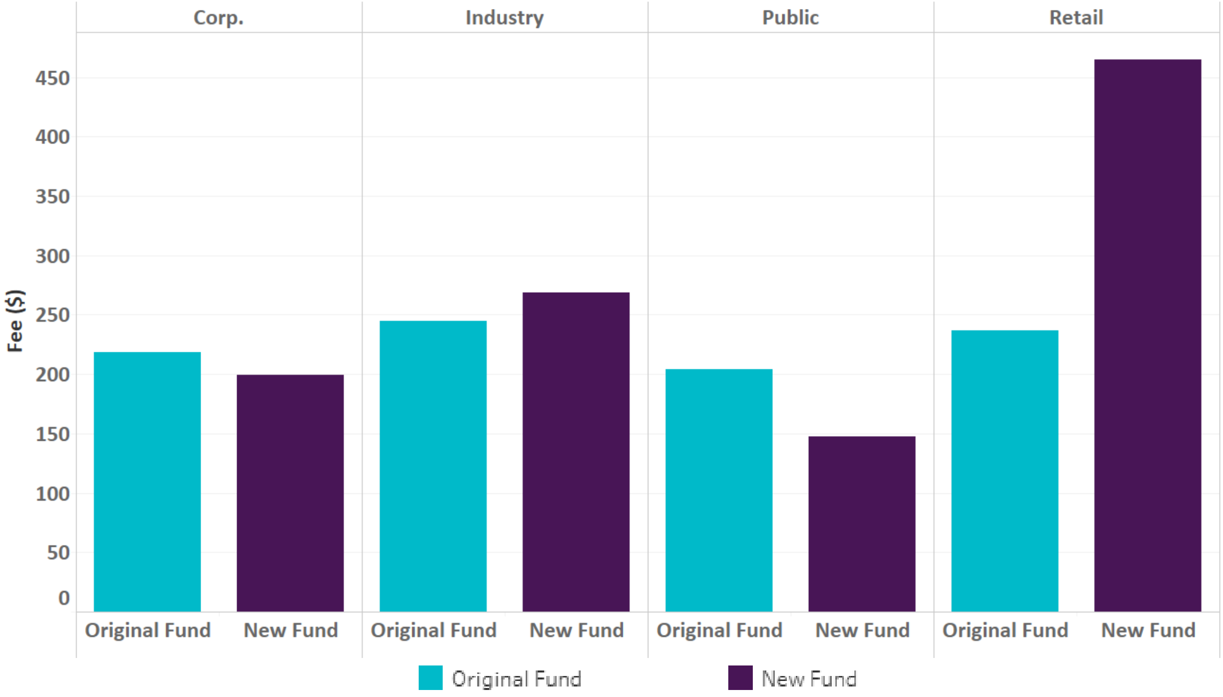
In an efficient market, it would be reasonable to expect that members would be motivated to seek out lower cost superannuation products or those that are likely to deliver higher returns based on their track record. In the context of member switches, we have compared fees and investment returns before and after member rollovers, to examine whether members make informed decisions to rollover to another fund based on these outcomes. We have not considered insurance, access to investment options or member services as part of this analysis, but given the primary purpose of the superannuation system to maximise people's retirement savings, this is a valid focus.

3.3.1 Fees

Fee levels across the industry have remained a focal point for consolidation and rollover campaigns for a long time. Members need to keep overall fee levels in mind and try to balance fees against the performance and services provided by a fund, due to their significant impact on retirement balances over time.

Graph 16 shows the average total fees paid by a member split by destination sector. The fees are shown both before and after the switch. Average total fees are comprised of a set dollar fee, an asset based administration fee and an asset based investment management fee.

Graph 16. Average total fee paid by destination sector



*Retail employer plans have been excluded from analysis as the level of discount provided is unknown. Hence the 'Retail' sector represents personal superannuation products only.

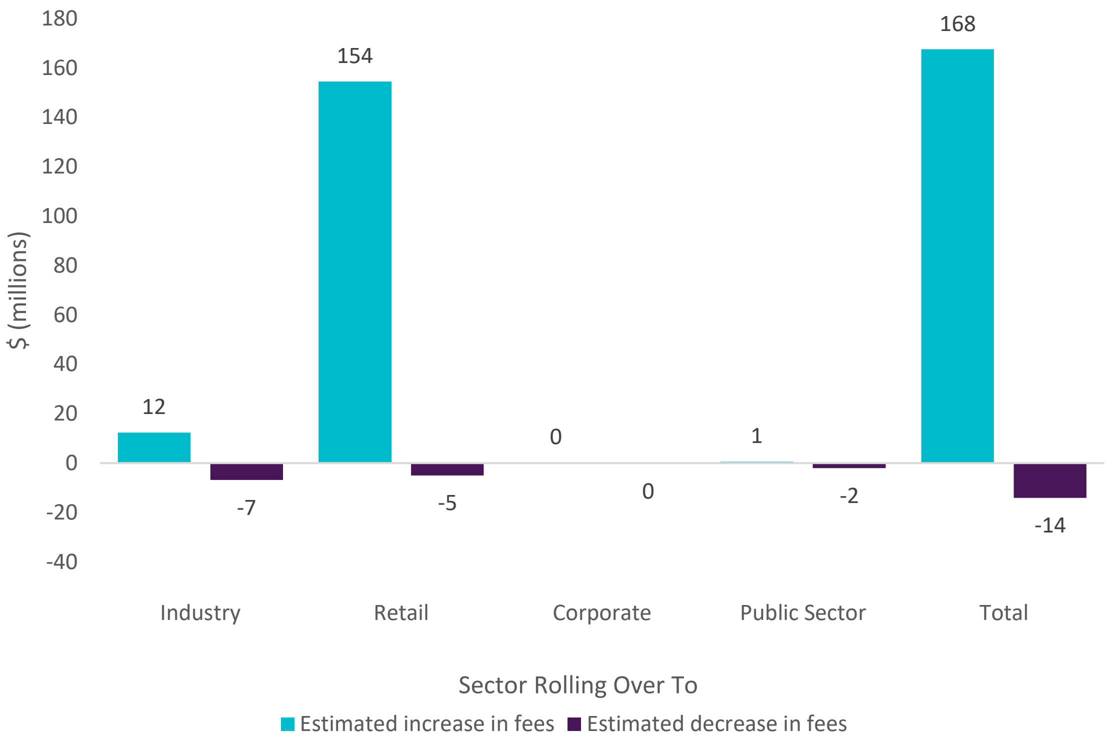
Source: Supeannuationr Insights 2015.

Based on the Insights data, the experience of members who rollover varies by destination sector. Overall new fund fees are lower in the public and corporate sectors driven mainly by their non-public offer status and employer fee subsidies. Fees are marginally higher in the industry fund sector, which are mostly public offer, and they are significantly higher in the retail.

Most notably, the increase in fees when switching to a retail fund is much higher than other destination sectors. On average, total annual fees double, increasing by approximately $200 when switching to a retail (personal superannuation) fund. This is primarily due to the switches to retail in our sample which come mainly from not-for-profit funds.

Graph 17 shows the estimated aggregate increase in total fees for members who rolled over to funds with higher fees, and the estimated decrease in total fees for members who rolled over to funds with lower fees, based on APRA statistics and the Superannuation Insights sample, for the year ending 30 June 2015.

Graph 17. Aggregate increase and decrease in fees paid by sector $M – 30 June 2015



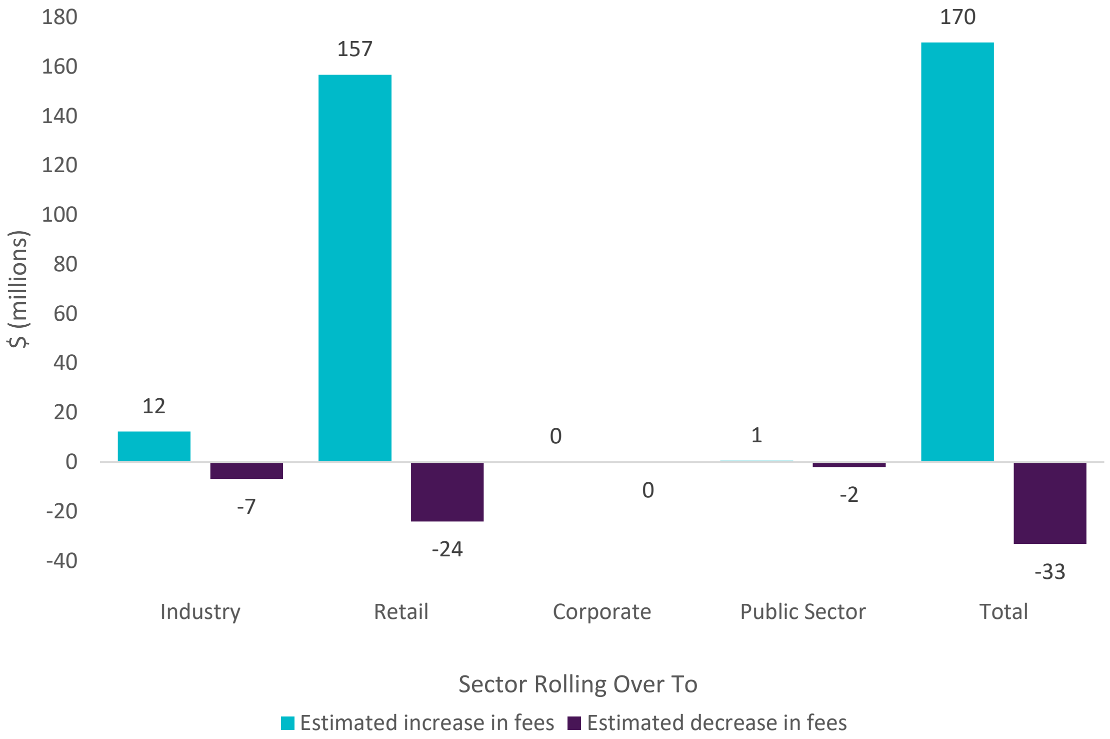
**Retail fee decreases do not include the decreases from rolling over into Retail Corporate Plans, due to the practice of providing discounts to PDS rates.*

Source: Rice Warner estimate using APRA Fund Level Statistics and Superannuation Insights 2015.

Members rolling into industry funds paid an estimated $12 million more in fees with savings of approximately $7 million for those who moved into funds charging lower fees. The higher fees for those switching to industry funds may be explained by the Superannuation Insights sample being dominated by larger (lower cost) industry funds reporting their exits to smaller (slightly higher cost) industry funds. Members rolling into retail funds paid an estimated $154 million more in fees with savings of approximately $5 million for those who moved into funds charging lower fees, though this estimate excludes potential cost savings that members may have experienced when moving into a corporate superannuation plan with a retail provider.

Graph 18 shows the aggregate increases and decreases in fees including employer sub-plan discount estimates (methodology detailed on the next page). We can see a slight adjustment in the retail numbers, with an estimated $157 million more in fees, and savings of approximately $24 million for those moving into funds charging lower fees. This is a net increase in fees of $133 million for those members rolling over into retail funds.

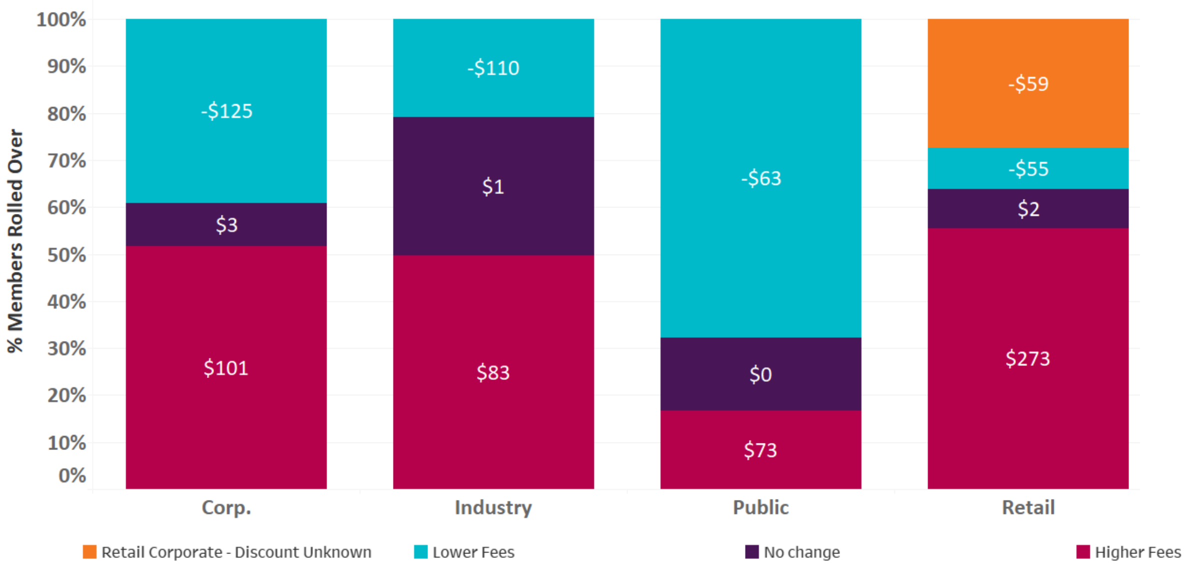
Graph 18. Aggregate increase and decrease in fees paid by sector $M (including employer sub-plan discount estimates) – 30 June 2015



Source: Rice Warner estimate using APRA Fund Level Statistics and Superannuation Insights 2015.

Graph 19 shows the member outcomes of rolling over to different sectors in terms of the percentage of members who received an increase, decrease or no significant change in fees.

Graph 19. Member outcome of rollover



Note: the dollar labels indicate the average change in fees for each group of members.

Source: Superannuation Insights 2015.

When rolling over to an industry fund, approximately half of members either experienced a drop in fees or no effective change in fees ($10 either way). For those rolling over to industry funds and realising a saving in fees, the average saving was $110. In contrast, the average saving for those rolling over into retail funds (not including corporate plans) was $55. The equivalent figure for corporate sub plans is estimated as $59. Conversely, for those rolling over to industry funds with higher fees, the average increase was $83, compared to an average increase of $273 for those rolling into retail funds.

Of rollovers to retail funds 27% of the rollovers were to corporate plans where the fees are unknown due to the practice of providing discounts to PDS rates. For those rollovers where fees are known, members did not fare as well with just 9% of total members who rolled over to retail funds experiencing lower fees.

Table 1 shows the proportion of members who paid lower fees, split by the sector rolled over from and to, while Table 2 shows the proportion of members who paid higher fees.

Table 1. % of members paying lower fees by sector

From	Industry	Retail	Grand Total
To		(%)	
Corporate	39	57	39
Industry	18	78	21
Public Sector	67	94	68
Retail	7	22	9
Grand Total	**19**	**51**	**20**

Source: Superannuation Insights 2015.

Table 2. % of members paying higher fees by sector

From	Industry	Retail	Grand Total
To		(%)	
Corporate	53	26	52
Industry	52	6	50
Public Sector	17	3	17
Retail	57	23	54
Grand Total	**51**	**14**	**49**

Source: Superannuation Insights 2015.

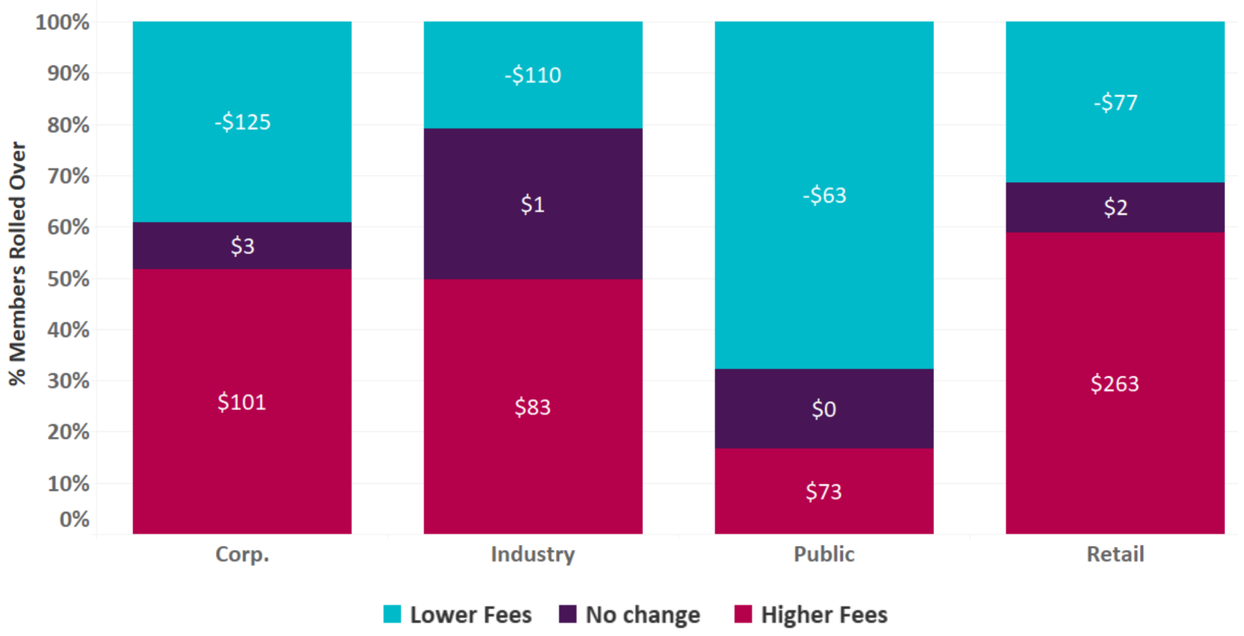
From Tables 1 and 2, we can see that 19% of members rolling out of industry funds move into funds that charge lower fees, while 51% move into funds that charge higher fees. Conversely, 51% of members rolling out of retail funds move into funds that charge lower fees, while 14% move into funds that charge higher fees.

Further, 21% of members rolling into industry funds pay lower fees, against 50% of members paying higher fees. For members rolling into Retail funds, only 9% of members pay lower fees, while 54% of members rolling into retail funds pay higher fees.

By making use of APRA MySuper Statistics, an estimate for those in employer sub-plans can be obtained. We have compared these estimates against our own experience in running tenders for corporate superannuation business. The level of discount varies by provider, but our estimated discount on average was 33% of total fees.

We have applied the average level for sub-plans for which data was not included in the MySuper statistics. Using this methodology, we have estimated that approximately 80% of members rolling over into an employer sub-plan experience a reduction in fees.

Graph 20. Member outcome of rollover (with estimated corporate plan fee discount)



Source: Superannuation Insights 2015.

3.3.2 Investment Returns

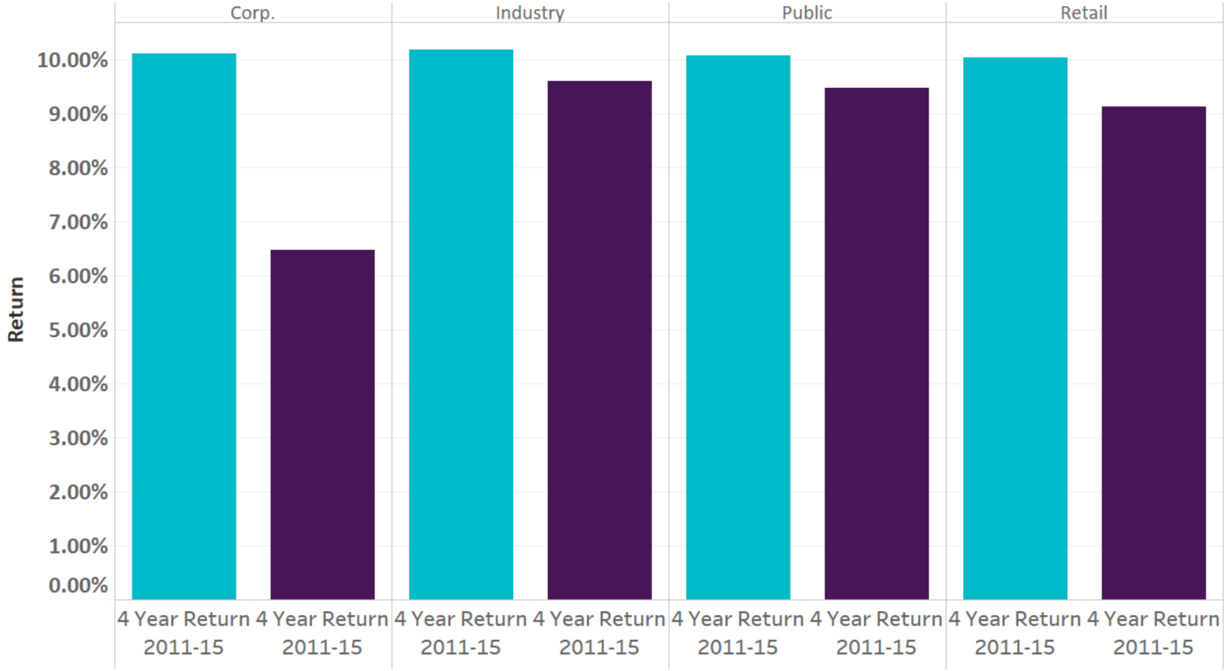
Fund investment performance is another major factor which dictates member outcomes. There have been suggestions that members should switch to high performing funds to maximise their outcomes. While we note that past performance is not a guide to future performance, we do know that funds which perform consistently well over the long-term tend to have robust governance and strong asset allocation. In these cases, they are more likely to perform well in the future relative to their peers.

We expect that many members would use past performance as a proxy to guide their switching decisions.

Although we are unable to predict the investment returns of funds in the future, we can compare how members would have fared based on historical returns.

Graph 21 illustrates the average investment returns for both the incumbent and successor funds where the performance was lower for the successor fund, split by destination sector.

Graph 21. Difference in historical returns for those members moving to a fund with lower 4y returns



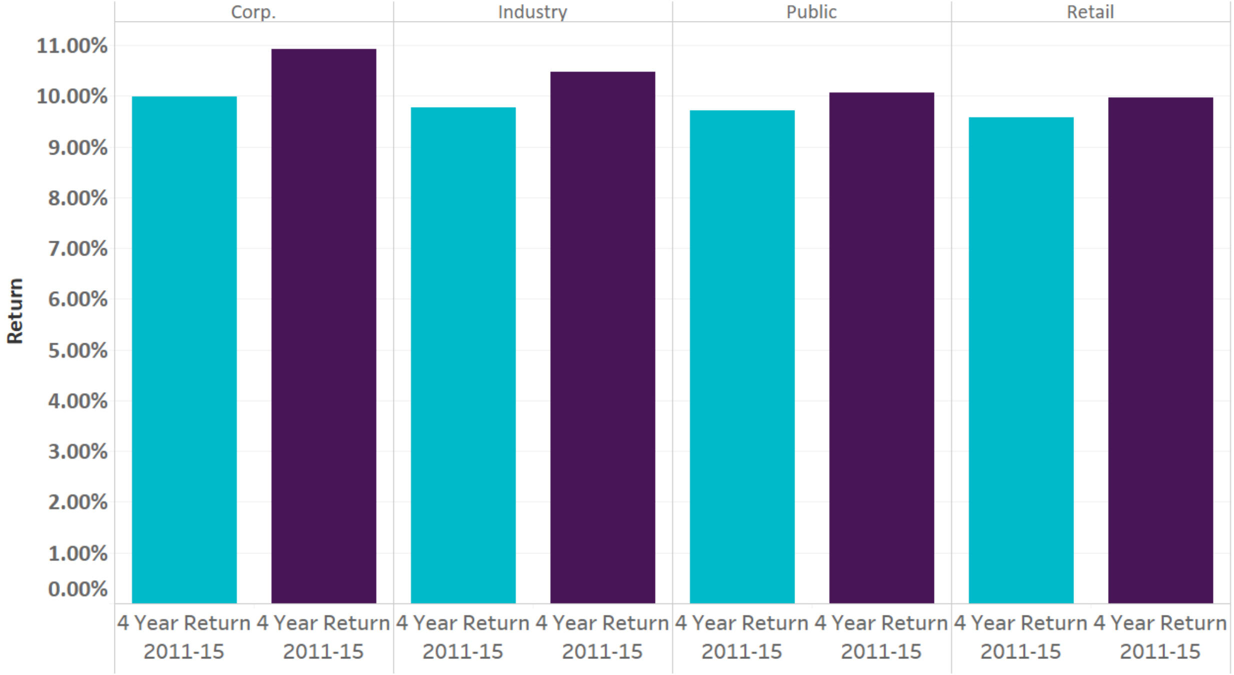
**Light blue represents the members' original fund and dark blue represents the fund rolled over to.*

Source: Superannuation Insights 2015.

This analysis is based on four-year annualised returns to 30 June 2015. The average historical performance for those rolling over to industry and public sector funds was approximately 0.5% p.a. lower than in the incumbent fund, whilst the equivalent figure for those rolling into retail funds was approximately 1% p.a. lower. Although this period is too short to conclude that these differences in results would continue, it does show that many members who switched have not done well in the period following the switch.

Graph 22 illustrates the average investment returns for both the incumbent and successor funds where the performance was higher with the successor fund, split by destination sector.

Graph 22. Difference in historical returns for those members moving to a fund with higher 4y returns



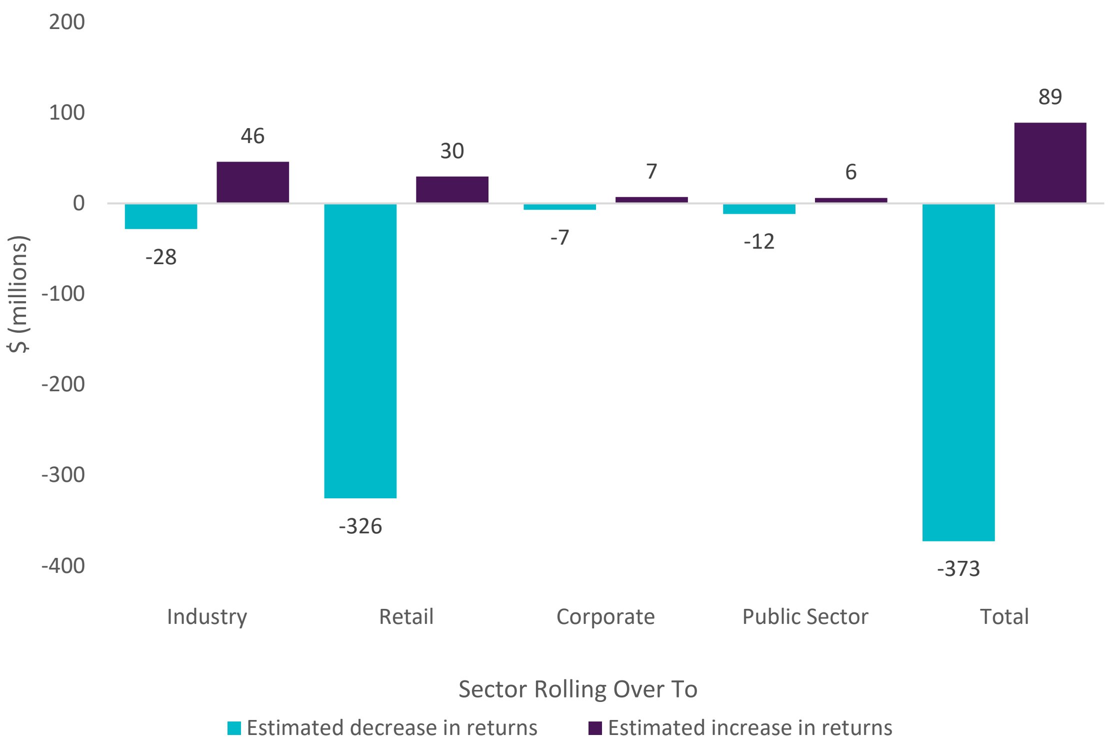
**Light blue represents the members' original fund and purple represents the fund rolled over to.*

Source: Superannuation Insights 2015.

The average historical performance for those rolling over to industry funds was approximately 0.7% p.a. higher than in the incumbent fund, whilst the equivalent figure for those rolling into retail funds was approximately 0.4% p.a. higher.

Graph 23 shows the estimated aggregate increase in four year investment returns for members that rolled over to funds with higher returns, and the estimated decrease in four year investment returns for members that rolled over to funds with lower returns, based on APRA statistics and the Superannuation Insights sample, for the year ending 30 June 2015.

Graph 23. Aggregate annualised impact on member balances of differential returns by sector ($M) June 2015



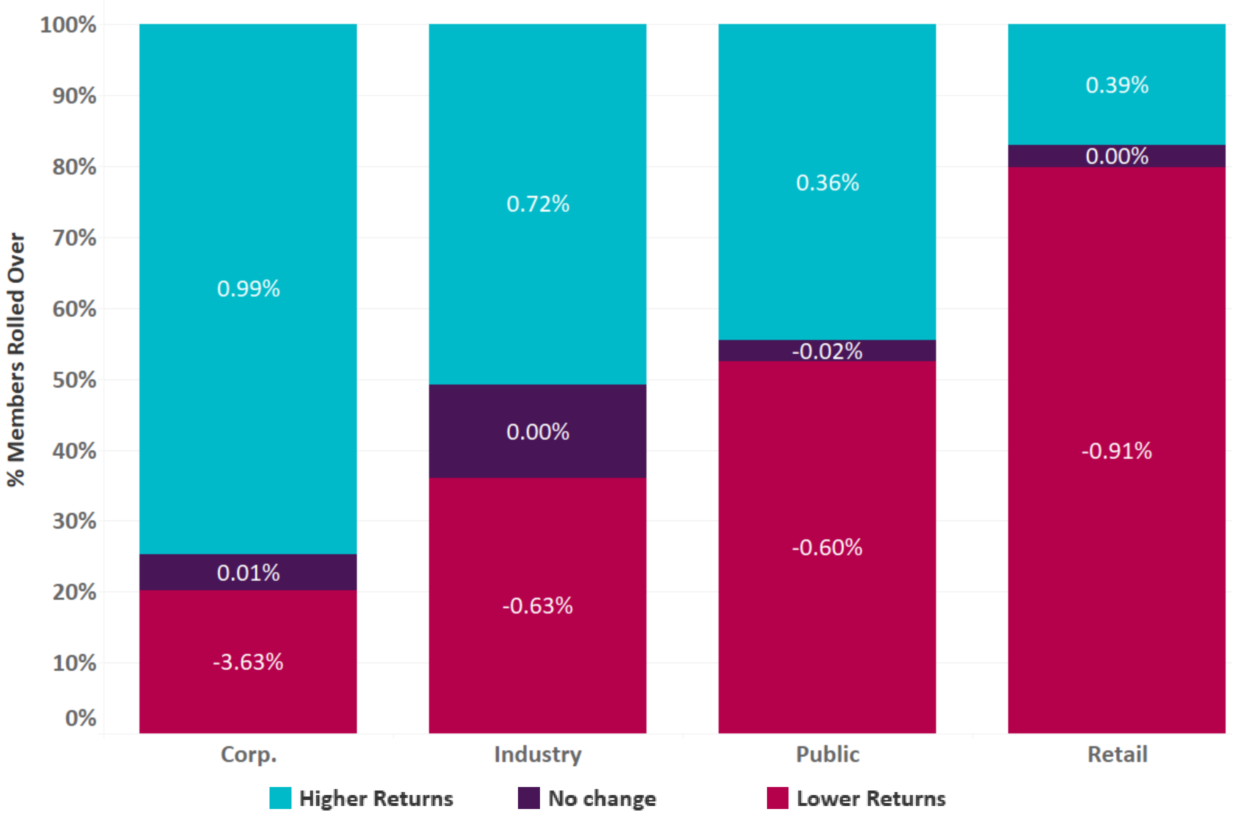
Source: Rice Warner estimate using APRA Fund Level Statistics and Superannuation Insights 2015.

Members rolling into industry funds would have received an estimated annualised increase in returns of $46 million, against an estimated decrease in returns of $28 million when moving into funds with weaker performance. Members rolling into retail funds would have received an estimated annualised increase in returns of $30 million, against an estimated decrease in returns of $326 million when moving into funds with weaker performance. This is a net decrease in annual investment returns of $296 million for those members rolling over into retail funds.

Note these estimates are based on historical performance applied to switching assets from APRA at 30 June 2015.

Graph 24 illustrates the proportion of member rollovers that are had better past performance split by sector. The comparisons are based on four- year investment performance to 30 June 2015.

Graph 24. Historical investment returns for exited members by destination sector



Source: Superannuation Insights 2015.

A change in investment performance of less than 5bps was included in the ‘no change’ category for this graph. Note that we have assumed the member invested in a similar option on switching to the new fund though it is likely that many members did choose a different investment strategy.

We note that 51% of members switching to an industry fund had a historically higher four-year investment return outcome, whilst 17% of members switching to a retail fund had historically higher investment returns.

Table 3 shows the proportion of members who moved to a fund with higher four year returns after rolling over, split by the sector rolled over from and to.

Table 3. % of members achieving higher returns by sector

From	Industry	Retail	Grand Total
To		(%)	
Corporate	74	80	75
Industry	52	23	51
Public Sector	46	*	45
Retail	17	13	17
Grand Total	**37**	**17**	**36**

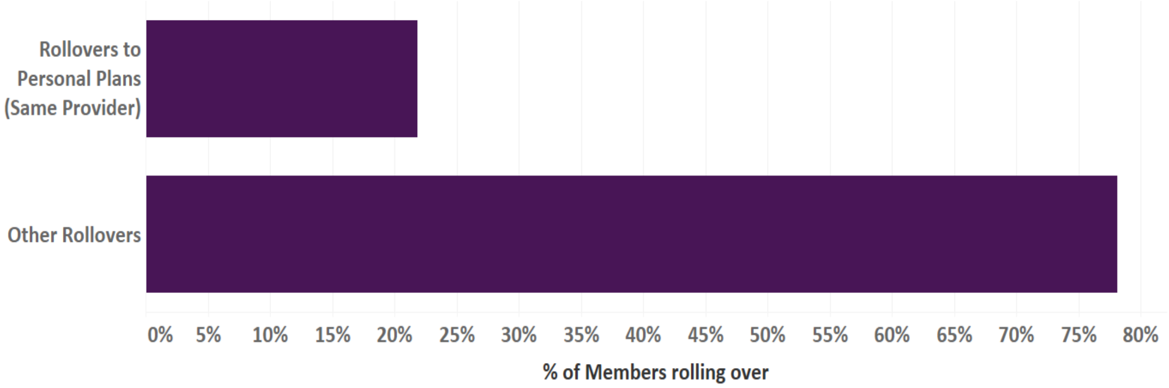
**Data is unavailable.*

Source: Superannuation Insights 2015.

3.3.3 Transfers from Corporate to Personal Superannuation

Of exits from retail funds, we observed a 22% rate of flips from retail employer plans to personal plans. This rate is an indicator of the level of default business that converts to Choice each year relative to total rollovers.

Graph 25. Retail flipping rate – Superannuation Insights sample

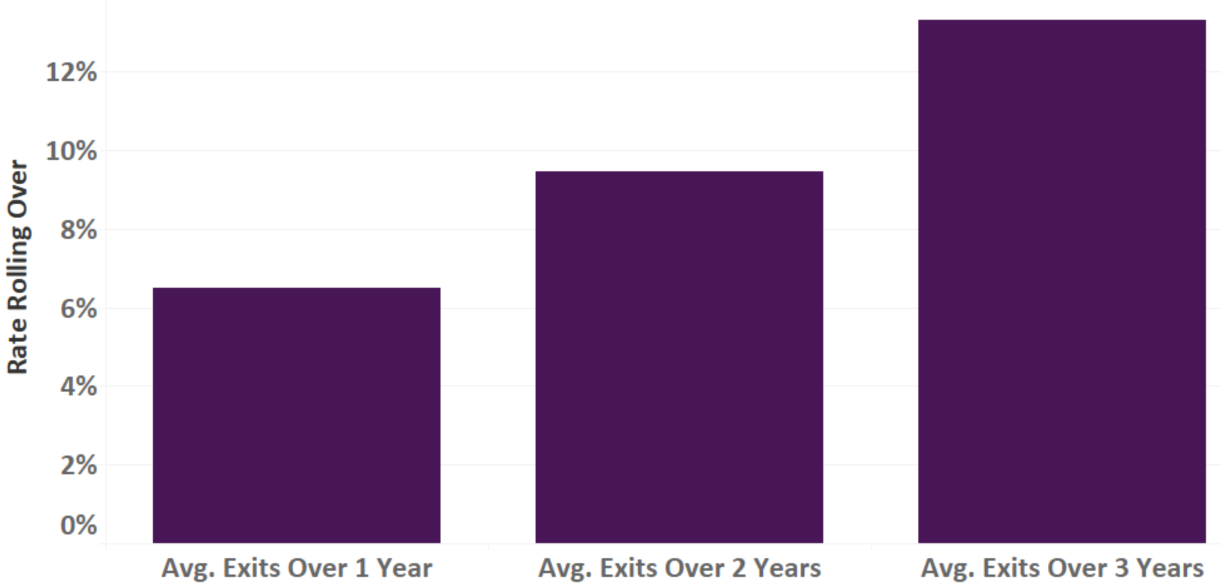


Source: Superannuation Insights 2015.

3.4 Cumulative rate of exit

We have further analysed what the cumulative rate of exit is for members over a period of three years by controlling the population at the start of 2013 and observing those members who left over a three year period (where data is available). From this analysis, we find that the probability of a member leaving a fund over a three year period is approximately 13%.

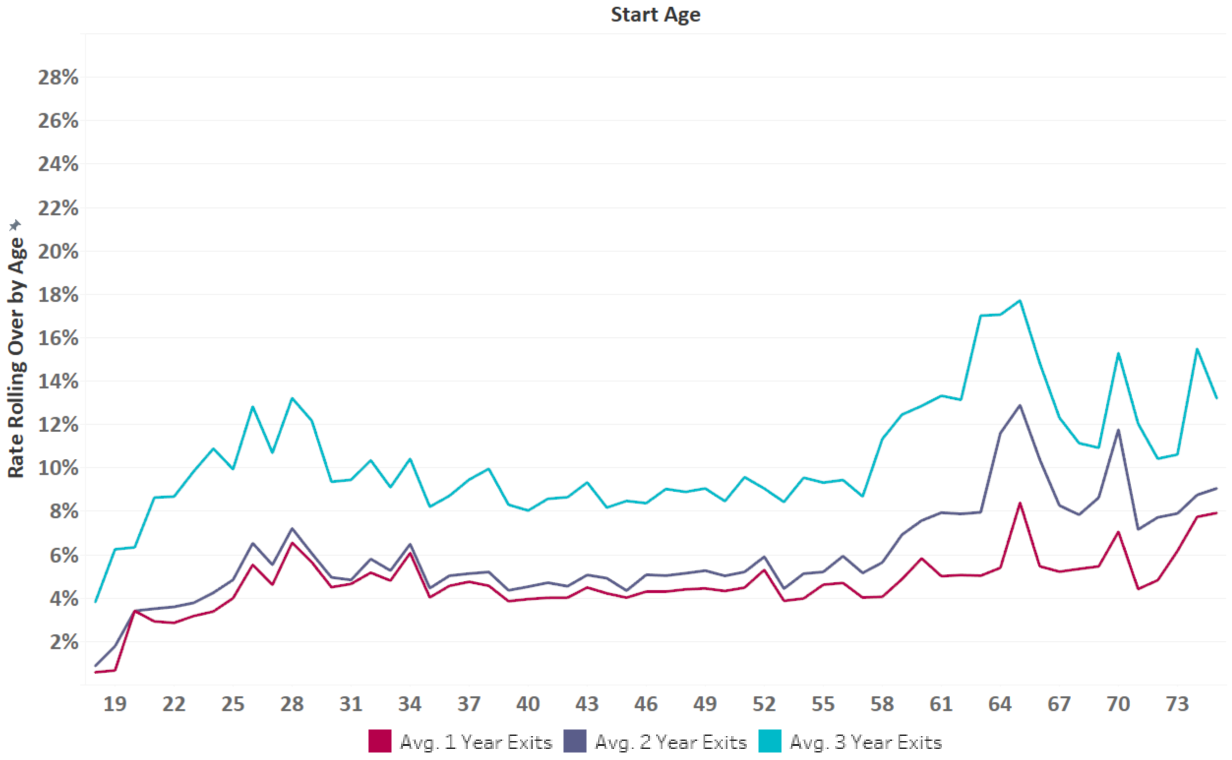
Graph 26. Cumulative rate of exit – 3 years



Source: Superannuation Insights 2015.

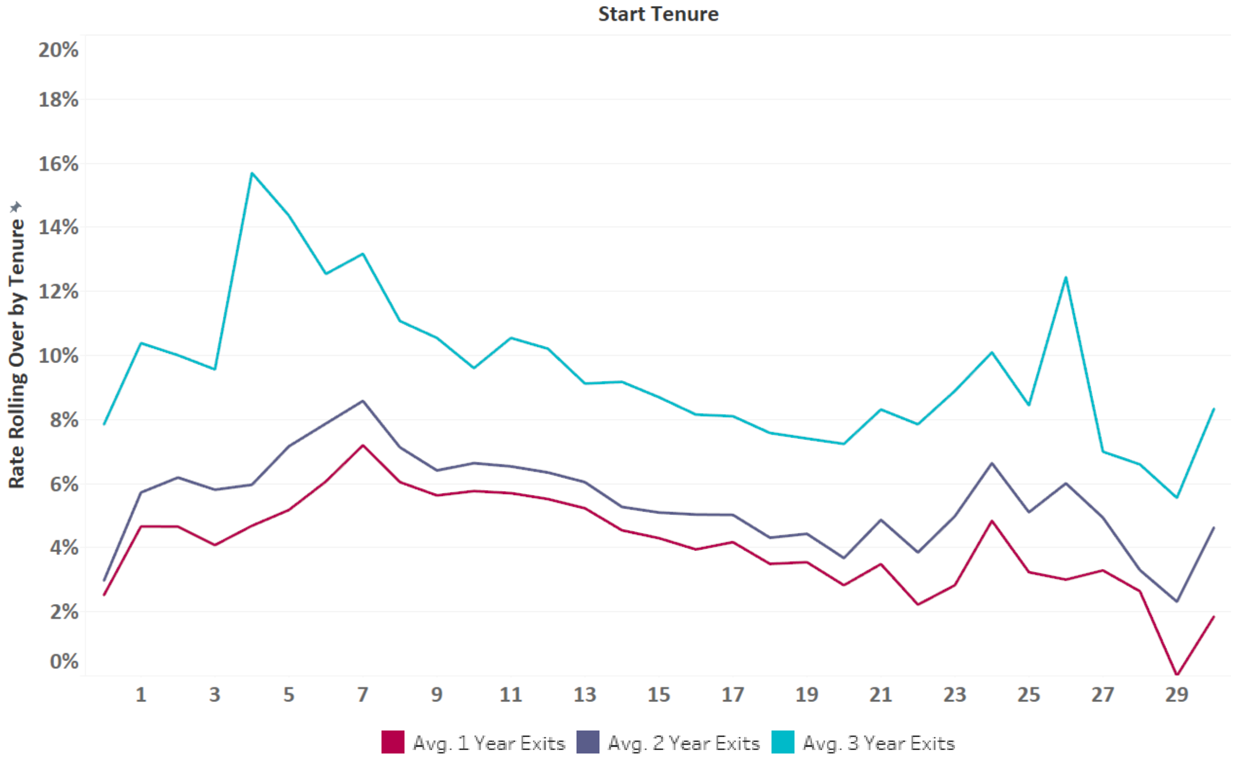
Graph 27 and Graph 28 show the cumulative rate of exit by age and tenure respectively.

Graph 27. Cumulative Exit probability by age over 1, 2 and 3 years



Source: Super Insights 2015

Graph 28. Cumulative Exit probability by tenure over 1, 2 and 3 years



Source: Super Insights 2015