

# CORPORATE SUPERANNUATION ASSOCIATION Inc.

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9 September 2016

Ms Karen Chester and Ms Angela MacRae  
Superannuation  
Productivity Commission  
Locked Bag 2  
Collins Street East  
Melbourne VIC 8003

Dear Ms Chester and Ms MacRae

## **RESPONSE TO DRAFT REPORT OF THE COMMISSION, AUGUST 2016 ON HOW TO ASSESS THE COMPETITIVENESS AND EFFICIENCY OF THE SUPERANNUATION SYSTEM**

We refer to the invitation to provide input on the Draft Report. Thank you also for the opportunity to participate in the Round Table meeting on 1 September 2016.

### **The Corporate Superannuation Association**

Established in 1997, the Association is the representative body for large corporate not-for-profit superannuation funds and their employer-sponsors. The Association now represents a total of 22 funds controlling \$72 billion in member funds, held in a total of some 560,000 individual accounts. Of these funds, 12 have outsourced trustee services but maintain significant employer interest through policy committees. In general, these funds are sponsored by corporate employers, with membership restricted to employees from the same holding company group, but we also include in our membership two multi-employer funds with similar employer involvement and focus.

A number of our funds have defined benefit divisions.

Size, in terms of funds under management, ranges from \$49 billion to \$64 million as at 30 June 2015. Some of the smaller funds have their place in the pension fund structures of international groups, hence play an important role in the care and welfare of the worldwide workforces of these groups.

### **Draft Report**

We recognise and appreciate the very thorough approach which is proposed. We believe that this will provide an opportunity for fair evaluation of the role played by the various participants in the industry.

# CORPORATE SUPER ASSOCIATION

## Objectives of the Superannuation System

We understand there is a view that the Productivity Commission should accept as a primary objective the Federal Government's primary policy objective for superannuation of providing income in retirement to substitute for, or supplement, the Age Pension.

We acknowledge that, for the purposes of the Productivity Commission's review of the superannuation system, objectives may be identified that are more detailed than those set by the Federal Government as policy objectives. We believe that it is helpful, as in the Draft Report, to provide separate references to key objectives of the system.

We support modification of these proposed objectives to reflect the following:

1. The optimisation of net returns  
This is an important stepping-stone towards the provision of retirement income or benefits. We prefer the term "optimisation" to "maximisation", as this takes into account that the balance between risk and return may be a matter of preference for a particular population.
2. The meeting of member needs and preferences, in particular in respect of retirement outcomes and retirement income stream products  
This acknowledges that the needs and preferences of members in retirement are diverse. As indicated in the Round Table discussion of 1 September, the focus on the provision of income in retirement is becoming the paramount consideration.
3. We also support the prominent inclusion of insurance in a study of the efficiency of the superannuation system. Our reasons are set out in detail below.  
We suggest modification of the proviso in the proposed objective from "meeting members' needs at least cost" to "meeting members' needs at an appropriate and sustainable cost". It is important that costs not be driven to levels where the providers are unable to sustain the benefits.
4. We do not believe that the inclusion of the fourth objective, of complementing a stable financial system, and not impeding long term improvements in efficiency, needs to be stated in this context, as an efficient system focused on the provision of benefits in retirement should in any case perform these functions as a by-product.
5. We accept that superannuation fund investment activities provide finance for many public projects and for Australian industry, but we believe that this should occur because such projects and industry provide appropriate investment opportunities that are valuable as part of the investment strategies of the funds. We firmly believe that the provision of finance for such projects should not be mandated.
6. We support the view stated in the Draft Report at page 65, and following, that competition is desirable not as an end in itself but only to the extent that it increases efficiency in promoting the objectives of the system.

The above objectives 1 to 3 and 5 are areas where potential efficiencies can be separately identified and tested.

We propose system-level objectives modified, as follows.

- The superannuation system optimises net returns on member contributions and balances over the long term.

# CORPORATE SUPER ASSOCIATION

- The superannuation system meets member preferences and needs, in relation to information, products and risk management, over the member's lifetime, with a strong focus on member-appropriate retirement outcomes and income streams.
- The superannuation system provides insurance that meets members' needs at an appropriate and sustainable cost.
- Competition in the superannuation system that drives efficient outcomes for members is encouraged.

## **Insurance**

The provision of suitable insurance, as an additional objective, reinforces the Federal Government's objective of providing income in retirement to substitute for, or supplement, the Age Pension. This is because insurance can be used in superannuation to cover the funding gap for required income and retirement benefits (including members' dependants' benefits) caused by premature death or by disablement. The covering of these gaps reduces burdens on the Social Security system.

Further, the policy approach to include insurance in superannuation provides many advantages and efficiencies. The effort in planning and obtaining such cover as an individual is generally a serious obstacle. Many people who would otherwise have no life and disability protection are protected under their fund without effort. The experience of corporate employers with the needs of their work force, and the ability to negotiate in relation to group profile and experience, increases efficiency in this area. In corporate funds, rigorous identification of needs, tender processes and evaluation promote efficiencies.

Further efficiency is introduced by provision of insurance through superannuation, in the form of reduction in administrative costs, as a result of economies of scale and of fund or employer negotiation power. Taxation savings also exist as a matter of policy, and it is efficient to benefit from these.

We acknowledge that problems of efficiency arise, particularly in funds where the employer's connection to members is more tenuous. Multiple policies arise where there are duplicate accounts, and the cost of ongoing insurance can erode benefits in inactive or duplicate accounts. In addition there are problems of adverse selection.

We support measures to contain these problems, and a range of solutions is adopted by our funds. We remain firmly of the view that the appropriate use of insurance in occupational superannuation arrangements promotes the overall aim of providing income in retirement from the workforce, to substitute for or to supplement the aged pension (or other government support).

## **Segmentation of analysis**

We support strongly the recognition that superannuation providers and products are not homogeneous. We believe that efficiency testing of disparate groups will enable more effective comparisons and recognition of valuable aspects of sectors.

We suggest that it may be helpful to compare the efficiency of funds stratified by governance structure to endeavour to discover whether benefits emerge from or are correlated with particular governance models.

# CORPORATE SUPER ASSOCIATION

## **Competition and Efficiency**

We strongly agree that to promote competition is helpful only if it leads to greater efficiency. In certain circumstances, competition can reduce efficiency (for example, where entities feel impelled to increase promotional activities, thus raising costs in that area).

## **Impediments to Efficiency or Barriers to Competition**

In relation to the discussion in Chapter 5 of the Draft Report of supply side barriers, we remind the Commission that certain barriers are caused by:

- regulatory intricacy and cost: there are advantages in excluding from the market those players who are ill-equipped to operate, but a general policy commitment to reduce the number of players, when implemented in a way that raises disproportionate cost barriers for smaller players, may result in collateral damage to some valuable arrangements;
- cumbersome regulatory and taxation classification arrangements, for example in relation to transition processes from accumulation phase to retirement phase;
- taxation anomalies and obstacles: noteworthy, the hitherto adverse treatment of deferred annuities, delaying the development and introduction of products which will fill gaps in the market.

## **Costs**

We agree that tracking all costs is going to be impossible, given the various ways in which costs find their way into the investment and fee hierarchies. A primary focus on competition on costs may be impossible to achieve. Furthermore, we agree that minimising costs may result in reduction in performance where there is a higher price for higher performance or for selections preferred by members. We support an approach that recognises that higher costs may yield greater returns. For this reason we support the proposed net returns approach.

## **Risk profile**

We have issues with the view that the adoption of long-term returns as an overall comparator removes the need to attach a risk profile to returns. Given the difficulties of measuring and reasonably comparing long-term returns, we believe it more helpful to evaluate and compare returns across segments stratified according to risk profile.

## **Conclusion**

We are happy to provide further information as required. Our particular experience lies with employers' continuing involvement in the management of their corporate funds, the particular governance strength in these arrangements, and in defined benefits arrangements.

Yours sincerely

**Mark N Cerche**  
Chairman