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21 October 2022

Your Future, Your Super Review – Consultation Paper

Thank you for the opportunity to provide a submission to the Your Future, Your Super Review (the review) Consultation Paper.

Australian Retirement Trust was formed through the merger of Sunsuper and QSuper on 28 February 2022. We are one of Australia's largest superannuation funds, managing approximately $220 billion in retirement savings for close to 2.2 million members.

Australian Retirement Trust supports the principle of holding funds to account for outcomes. Further, we believe in assisting members to make informed decisions about their superannuation, and where member choice is not possible, to provide high quality default products.

We have observed the operation of the Your Super, Your Future reforms and are pleased to participate in the review. We reinforce in this submission that:

- The Performance Test has had a positive impact on the industry and will help to deliver better retirement outcomes for more Australians.
- The universe of asset class benchmarks should be expanded to better reflect the broader range and purpose of Trustee Directed Products (TDPs) offered by the industry, including sustainable investment options, before expanding the Performance Test coverage to include TDPs.
- The scope of the Performance Test for TDPs should be restricted to include diversified multi-asset options and exclude multi-region single asset class options.
- A performance assessment framework for products not currently captured by the Performance Test, including retirement products, should be developed.
- The consequences of failing the PT have been effective in driving consolidation of funds, however, has been less effective in driving members to switch to a fund that has better comparative performance.
- The prescribed information provided to members and the YourSuper Comparator Tool may not provide a holistic view, does not empower members to make an informed choice and could lead to unintended outcomes.
- The combination of efficient and effective options (including onboarding software solutions), and effective enforcement should drive greater employer compliance with stapling requirements.
- The reverse onus of proof, associated with acting in the best financial interests of members, has created uncertainty as to the obligations placed on trustees with respect to decision making, including some uncertainty as to the ability of a trustee to seek innovative solutions for the benefit to its members into the future.

We trust this feedback will be beneficial to Treasury's considerations and would welcome the opportunity to discuss our submission in further detail.

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Yours sincerely,

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Your Future, Your Super Consultation Paper - Australian Retirement Trust responses

<u>**Performance Test - Methodology**</u>

1. Does the measurement of actual return using strategic asset allocation affect risk taking behaviour by superannuation trustees?

2. Does the current set of indices used to calculate benchmark returns unintentionally distort investment decisions or reduce choice for members? If so, is there a way to adjust the benchmark indices while maintaining a clear and objective performance test?

3. Does the calculation of actual RAFE and benchmark RAFE discourage non performance related product features that members may value (such as customer service or platform products)? If so, can this be addressed without diminishing the test's focus on performance?

4. What are the longer-term impacts of the performance test on market dynamics and composition? How will these factors impact on long-term member outcomes?

1. Does the measurement of actual return using strategic asset allocation affect risk taking behaviour by superannuation trustees?

The introduction of the Performance Test (PT) has elevated trustee awareness and oversight of active risk and benchmark relative performance across all multi-sector diversified superannuation investment products and within the asset classes that underpin those products. Greater awareness of those risks has the benefit of improving trustee's governance and oversight of active risk within portfolios and improving accountability in terms of the outcomes received by members relative to the investment fees and costs incurred.

An increased focus on active risk has in some cases required a decreased focus on total risk for some investment options. The increased focus on active risk has also in some cases reduced the appetite for trustees to take large deviations from strategic asset allocations.

2. Does the current set of indices used to calculate benchmark returns unintentionally distort investment decisions or reduce choice for members? If so, is there a way to adjust the benchmark indices while maintaining a clear and objective performance test?

The limited range of benchmarks applied in the PT coupled with uncertainty about the future application of the PT has led to what ART believes are some unintended consequences in terms of investment decision making and member choice:

<u>Product Choice</u>

The breadth of choice product menus across the industry will inevitably reduce in response to the PT. While some of this reduction is an intended consequence caused by underperforming products closing, there is also an incentive for trustees to limit choice menus to only incorporate asset classes that are defined by the test. Given the uncertainty of the future application of the PT, and the history of it being applied retrospectively, even options that are not currently included in the PT represent potential future risks and we believe this can lead to unintended constraints on choice. Examples include:

- The existence of a PT has the potential to reduce the appetite for trustees to offer single sector options that deviate from the narrow range of offerings defined under the YFYS regulations.
- Single sector choice options that span multiple sub-asset class benchmarks such as fixed income options that are 50% Australian and 50% International are currently classified as TDPs and will be included in the PT. This incentivises trustees to either discontinue those options, or reduce their scope to being either 100% Australian or 100% International to avoid their inclusion in the PT.
- Uncertainty with respect to the future expansion of the PT to retirement income strategies may limit the capacity to offer innovative post-retirement investment solutions.

Recommendation: Definitively outline the scope of the PT now and into the future. We believe that this scope should exclude single asset class options, including options in a single asset class that span multiple sub-asset classes, and all options offered to members in pension accounts until such time as an alternative framework for performance assessment has been developed for these products, in consultation with industry**.**

Multi-sector product design

The limited range of asset classes defined in the YFYS regulations, coupled with the generic treatment of “Other” assets within the test has implications for investment decision making, some of which we believe are unintended:

- Undefined or ‘Other’ assets are treated as having a 50% Growth and 50% Defensive profile. This naturally incentivises trustees to focus on higher growth alternatives at the expense of defensive alternatives.
- Established asset classes such as Commodities, Inflation-linked bonds and International Unlisted Property are not recognised with appropriate benchmarks in the YFYS regulations, disincentivising trustees from including these diversifying assets, limiting trustees’ ability to diversify portfolios against inflation risk.
- Trustees are incentivised to implement active asset allocation strategies, such as trend following, internally through derivative overlays and are disincentivised from using external fund structures, even though those structures mitigate risk.
- Climate change is a complex systemic issue that will impact the global economy and create financial risks and opportunities. APRA has developed the *Prudential Practice Guidance CPG 229 Climate Change Financial Risks* (CPG 229) to assist its prudential entities in managing this risk. The PT may have the unintended impact of limiting superannuation funds from appropriately considering climate change within its investment strategy and creating mis-alignment with CPG 229 (e.g. mis-alignment on time horizons and absence of customised specialist asset class benchmarks).

Recommendation: Expanding the universe of asset classes with defined benchmarks to include:

- A Growth Alternatives asset class which has either an Australian or Hedged International Shares benchmark based on jurisdiction
- A Defensive Alternatives asset class which has either an Australian or Hedged International Fixed Income benchmark based on jurisdiction
- Specifying an appropriate benchmark for the International Unlisted Property asset class
- A broad Commodities asset class benchmark
- Both an Australian and a Hedged International Inflation Linked Bond asset class benchmark
- Using a Cash benchmark for market neutral long-short strategies, which would negate the incentive to use internally managed overlays to implement these strategies.

- Consideration could be given to customising the PT for specialist asset class benchmarks such as climate-aware equity benchmarks.

Nation Building Investments

The inclusion of unlisted asset benchmarks in the PT benchmark universe was an important improvement that Treasury implemented following the previous round of consultation which supports the ability for superannuation funds to support nation building investments. However, the inclusion of unlisted benchmarks in multi-asset SAA benchmarks can also introduce unintended disincentives which we believe are worth highlighting to raise awareness:

- Often nation building investments will have unique and differentiated characteristics which is generally an attractive feature of these investments. However, where these differentiated characteristics are not well reflected in an asset class benchmark, the PT could have the unintended implication of limiting the capacity of a fund to participate in an investment without exceeding the trustees risk appetite for active risk.

- Another challenge is associated with rebalancing unlisted benchmarks. The PT SAA benchmark receives a tailwind from transacting unlisted assets under/overweights when listed markets rise/fall. Unlisted asset benchmarks therefore penalise allocations to unlisted assets through rebalancing without giving any offsetting benefit for the illiquidity risk premium and the larger the allocation to nation building unlisted assets the larger the penalty.

Recommendation: These are not challenges with obvious solutions and we believe that unlisted benchmarks are a positive feature of the PT. As such we recommend Treasury maintains an awareness of these challenges and seeks a constructive ongoing dialogue with participants in the superannuation industry to proactively seek solutions to mitigate these disincentives should they begin to restrict investment in national building investments.

Investment Objectives and Choice

A diverse range of factors influence member investment choices and by not recognising these other objectives, the PT may have the unintended impact of limiting the ability of superannuation funds to offer products that suit these member needs:

- Objectives such as those pursued in Sustainable options are not well catered for in the test. These options could fail the PT while being consistent with member preferences when excluded stocks outperform over the PT measurement period.
- Historical poor performance relative to the test and the sequencing of returns could lead to an elevated focus on PT risk mitigation, rather than on delivery on primary risk/return objectives.
- The largest driver of member investment outcomes, asset allocation, is not measured by the PT. Through thoughtful design and consultation the current PT has produced, and should continue to produce, favourable outcomes for investment products with strong risk adjusted returns. However, as return for risk is not explicitly considered in the PT, this could limit the capacity for trustees to design portfolios with the aim of maximising risk adjusted returns.

Recommendation: Consideration could be given to customising the PT for some specialised investment options either through a differentiated overall objective such as a portfolio return-for-risk, (e.g. Sharpe Ratio) measure, or through specialist asset class benchmarks such as sustainable equity benchmarks.

3. Does the calculation of actual RAFE and benchmark RAFE discourage non-performance related product features that members may value (such as customer service or platform products)? If so, can this be addressed without diminishing the test's focus on performance?

Trustees have a Best Financial Interests Duty with respect to member outcomes. Thus, it is incumbent on trustees to ensure that administration and other non-performance related costs incurred by a member translate to better net member outcomes. ART believes that all costs that are deducted from a member's account should be included in the RAFE for the purpose of the PT to ensure trustees continue to act in members' best financial interests.

4. What are the longer-term impacts of the performance test on market dynamics and composition? How will these factors impact on long-term member outcomes?

The PT will have a meaningful positive impact on the industry and members by:

- Raising awareness and engagement with respect to superannuation choice.
- Identifying and eliminating underperforming products.
- Encouraging and accelerating consolidation within the industry.
- Incentivising funds to reduce fees to improve PT outcomes.

While some risks with respect to unintended impacts from the PT and potential mitigants are outlined above, ART supports the PT and underscores the view that the positive impacts from the PT outweigh these risks.

<u>Performance Test – Consequences of failure</u>

5. Is there evidence to indicate that the notification and website publication requirements have been effective at encouraging members to consider, and switch to, alternative products? Are there ways this could be improved?

6. Have the consequences been effective at encouraging trustees to improve their performance or merge with better performing funds? Are there ways this could be improved?

7. Are the measures in place to resolve underperformance sufficient given the potential for members to be stapled to these products? How can the system best support members in underperforming products?

5. Is there evidence to indicate that the notification and website publication requirements have been effective at encouraging members to consider, and switch to, alternative products? Are there ways this could be improved?

The notification has been effective at encouraging some members to take action to switch products. In September and October 2021, ART roll-ins from 10 of the 13 funds that failed the PT showed significant increases. In September and October 2022, ART is observing a similar increase in roll-ins from funds that failed the PT a second time. We note though the information in the consultation paper states that 90 per cent of the members who received the notification took no action.

There are ways to improve the notification for members:

- An approach that allows for more complete and tailored communications based on the fund's membership is preferred. In some cases, a member should not have to leave the fund to get a better outcome as there may be more appropriate choice investment options available. Therefore, the notification should empower funds to engage the membership on other suitable choice investment options and services available (such as an offer of Intrafund advice).
- The notification could also include warnings regarding unintended consequences of switches and rollovers, in the form of a checklist to protect members with a low level of financial literacy, who have never exercised choice.

6. Have the consequences been effective at encouraging trustees to improve their performance or merge with better performing funds? Are there ways this could be improved?

The consequences have been effective at encouraging trustees to consider a merger with 'better performing' funds:

- Resulting in industry consolidation of underperforming funds – evidenced by merger activity following the underperformance notifications (as stated in the consultation paper).
- However other factors that come into consideration include:
    - The expense and complexity associated with mergers.
    - The capacity for funds to perform Successor Funds Transfer (SFT) mergers (there is a limited number of administration providers in the market).
    - The Best Financial Interests Duty (BFID) of the receiving funds members being aligned to the proposed merger.
    - The challenge to provide equivalency in the receiving fund, across all members being transferred.

There may be ways to improve the effectiveness of the consequences by:

- Improving the Notification to invoke member choice.
    - Evidence as stated in the consultation paper indicates that members are not engaged with or called to action by the notification.

- Creating an efficacy in transference of underperforming funds, to improve the attractiveness to potential merger partners. This could be achieved through review of the SFT regime to make it simpler by addressing some of the regulatory barriers to SFT and considering trustee's existing duties as adequate protection of a transfer of this kind.

7. Are the measures in place to resolve underperformance sufficient given the potential for members to be stapled to these products? How can the system best support members in underperforming products?

The measures (consequences) may not be sufficient with the introduction of stapling because:

- Stapling requires a member to take action to move from an existing stapled fund.
- Low levels of engagement remain a challenge across the industry.
- As a result, the PT consequences continue to see the majority of impacted members exposed to underperforming funds, until a merger partner or fund exit can be established, or the member actively exercises fund choice.
- Impacted members may be exposed to underperformance for 2 years or longer under the current approach, where closing the fund to new members still leaves existing members at risk.
- Members are now concentrating their retirement savings in one or two accounts resulting in a potential for a larger exposure of retirement savings to underperforming funds.

<u>Performance Test – Product coverage</u>

8. Are there any significant issues to be expected when the test is extended to TDPs? If so, how could these issues be addressed?

9. What would be the impact of extending the current performance test to other Choice products (such as single sector or retirement products)? How could any issues be addressed?

8. Are there any significant issues to be expected when the test is extended to TDPs? If so, how could these issues be addressed?

Three potential issues may arise when the PT is expanded to TDPs:

- Sustainable investment options will face an elevated ongoing risk of failure due to a misalignment in option objectives with the PT.
- Some single sector options may be treated as TDPs and be subject to the PT contrary to the intent of the PT.
- Defensively oriented TDPs with allocations to defensive alternatives have been penalised for alternatives allocations through the "Other" benchmark and as such an elevated proportion of conservative TDP's may fail the PT.

Mitigants to these issues are proposed in response 2 above.

9. What would be the impact of extending the current performance test to other Choice products (such as single sector or retirement products)? How could any issues be addressed?

Extending the performance test to single sector options would effectively restrict trustees to only offering single sector options for asset classes that are defined in the PT benchmarks. Consequently Treasury, through the YFYS regulations, might effectively become responsible for legislating the allowable range of single sector options. ART does not believe that this is the intent of the YFYS and PT regulations and we do not support extending the PT to single sector options.

Retirement products serve a different purpose to accumulation products, i.e. converting capital to income (selling assets) and possibly pooling longevity risk (which is not an investment activity). This contrasts with accumulation products (buying assets) which simply aim to maximise capital wealth through risk-adjusted returns. As the PT currently does not distinguish the objective of the product (e.g. stability and sustainability of income), or risk employed/managed, ART believes it would be inappropriate to use the PT in its current format as a measure of success for retirement products. Furthermore, retirement products are likely to evolve in response to the Retirement Income Covenant and expectation that the current PT would be extended to retirement products could stand in the way of thoughtful evolution. For these reasons, ART does not support expanding the PT to retirement products at this stage.

ART advocates for APRA to develop, in consultation with industry, a performance assessment framework for products not currently captured by the PT, including retirement products.

<u>YourSuper comparison tool</u>

10. Does the comparison tool adequately inform members and prompt a behavioural response? Is the tool effective at informing new employees of their options when entering the workforce, including those who do not have an existing superannuation account?

11. To what extent would altered or additional metrics, or improved functionality, make the tool more effective while ensuring it remains simple and clear? What more can be done to ensure that new employees are able to choose high-performing superannuation product that are appropriate for their needs?

12. As the test is applied to more superannuation products, should the comparison tool also be extended? Considering the volume and complexity of Choice products, how could the tool be extended in a way that is meaningful and digestible to members?

10. Does the comparison tool adequately inform members and prompt a behavioural response? Is the tool effective at informing new employees of their options when entering the workforce, including those who do not have an existing superannuation account?

ART does not believe that the tool adequately informs new employees or members. We are unable to comment on behavioural response without data and insights into the users of the tool, why they used it and what behaviour may have resulted from use.

Whilst the comparison tool may have the intention of providing simple, accurate, accessible and comparable information from a trusted source, concerns about potentially inaccurate information (due to timeliness) and a lack of explanatory information mean the ATO comparison tool may expose consumers to some risk.

Some concerns are outlined below.

- Potentially inaccurate information

The data displayed by the tool is lagging in currency and may lack the transparency required to assist fund choice.

  - Data currency - The data may be up to 12 months out of date.
  - Transparency – Fee presentation for consumers with multiple accounts in the authenticated site is confusing. Consumers can be presented with a fee value which is higher than the balance of that particular account. This may be due to the total super balance across accounts being used in the fee calculation, however no explanation is provided.

- Tool logistics and risks

Superannuation by its nature is complex. It is difficult for the tool to have the sophistication required to provide a holistic and reliable comparison to guide consumer decisions and build knowledge. The tool may require further optimisation to drive an enhanced behavioural response.

  - Risk profiles are not considered. Further information and explanation of risk and return could help prevent harmful decision making for consumers.
  - Both net returns and fees are listed. As the tool states that the investment returns are net and inclusive of all fees may also be confusing to also list fees. This could lead the consumer to double count the impact of fees.

  - The investment horizon needs further explanation. It is unclear why an eight-year return period is selected. Funds typically display returns over 1, 3, 5, 7 and 10 year periods. Longer term periods are usually more suitable for long-term investments such as superannuation.
  - The comparator tool is inconsistent with the subsequently provided [via click through on comparison] MySuper Product Dashboards. The MySuper Product Dashboards include information on a product's return target and actual returns over a 10-year period. Consumers would benefit from a more consistent approach.
  - Funds offer different MySuper products. Both lifecycle MySuper products and single diversified MySuper products are offered by funds. Divergence occurs when lifecycle products de-risk closer to retirement age as more conservative investments are included in the investment portfolio. Lowering of risk generally [but not always] results in lower returns. However, this is not explained to consumers.
  - Lack of insurance information. While it may be difficult for the tool to consider this, it can form an important data point in fund selection. Consumers have varying high-risk and low-risk occupations and some funds cater to these needs, aligning with industry occupational risks.

11. To what extent would altered or additional metrics, or improved functionality, make the tool more effective while ensuring it remains simple and clear? What more can be done to ensure that new employees are able to choose high-performing superannuation product that are appropriate for their needs?

Based on assessments from ART's user and customer experience experts, our evaluation is that the user experience is poor, and the tool is not intuitive. We recommend user testing be undertaken. This could be based on best-practice behavioural science. There is a lack of overarching explanation to understand how the tool is to be used, understand the key datapoints or build financial knowledge. Concerns include:

- Lack of usability
- Lack of explanation of various data points
- Prefiltering set at $50,000 without explanation
- The filter is not easily located
- The default ordering of funds by fees. As the net returns take fees into consideration, it adds confusion. There is potential to order by net returns.

Improvements to the tool to provide a more holistic approach to better support decision making could include:

- Broader financial content to give context to the information provided and explain its importance in fund selection.
- More extensive information that enables consumers to identify a fund that meets their needs. For example:
  - Details regarding insurance offers and how to compare these
  - The addition of return-for-risk metrics
  - Explanation of the difference between single diversified and life-cycle funds.
- Greater clarity around measures such as net returns and fees.

The Productivity Commission[1] warned against providing more information rather than better information for consumers. We consider the tool does not provide better information than what currently exists for superannuation customers in existing comparison tools.

12. As the test is applied to more superannuation products, should the comparison tool also be extended? Considering the volume and complexity of Choice products, how could the tool be extended in a way that is meaningful and digestible to members?

Tool extension should take into account the trade-offs between simplicity and any consumer expectation that they are selecting from a full range of investment products. Key considerations for expansion include:

- Choice products are not easily comparable
- Consumers should potentially seek advice before choosing a Choice product. Consumers need to be able to factor in their personal situation if choice products are added.
- Consumers may not know the difference between a MySuper product and a Choice product
- Adding in retirement products, for example, could increase risk as consumers are highly likely to require comprehensive personal advice.

It is not clear how an extension of the tool will add value to the market and we recommend that the tool is optimised for MySuper products before an extension to Choice products is considered.

A number of independent comparison tools for superannuation products exist in the market. Some of these comparators provide holistic comparisons of super funds across multiple variables, products and services, with a good user experience. We would recommend more consultation with industry and consumers to guide an end-to-end solution that better helps consumers to make informed decisions.

[1] Productivity Commission Inquiry Report, Superannuation: Assessing Efficiency and Competitiveness, No. 91, 21 December 2018

Stapling

14. To what extent are employers putting into practice processes to seek stapled fund details from the ATO? How has the implementation of stapling changed onboarding, software and payroll processes for new employees?

15. Are there any barriers in the current framework to achieve the intent of the stapling reform?

16. What is the actual, or likely, impact of stapling on insurance coverage?

14. To what extent are employers putting into practice processes to seek stapled fund details from the ATO?

As a superannuation fund, ART does not have direct visibility of employers' choice and stapling behaviour. Our employer default sponsored membership inflows and churn trends do not yet show any meaningful reduction. This may suggest that a significant proportion of employers are yet to put into practice processes to seek stapled fund details from the ATO.

Default sponsored membership inflows are an indication of stapling behaviour. This is based on the fact the majority of members added already have an existing superannuation account and are unlikely to have chosen to join the fund directly via the employer. Therefore, if a significant proportion of employers were to have made stapled fund requests, the volume of inflows of new accounts should have reduced.

ART's experience with supporting employers through similar regulatory change, shows that a significant proportion of employers will not amend their behaviour until enforcement regimes are in effect.

Stapling obligations came into effect 1 November 2021, however legislative instruments[2] registered by the ATO in October 2021 outlined a transitional compliance approach for new stapling obligations which enabled employers to avoid penalties.

These legislative instruments and associated media coverage, in the absence of a perceived benefit, generally have the effect of postponing compliance. Similar behaviour was observed throughout the implementation of SuperStream and Single Touch Payroll reporting changes, where a significant proportion of employers delayed compliance until enforcement regimes were in effect.

We do believe that employers will comply with new regulations to a greater extent where efficient and effective options exist.

Stapling impacts employers already using onboarding software significantly less than employers onboarding via other methods. Digital onboarding processes generally require choice of fund before an employee can proceed or finalise their onboarding journey, and as a result lead to choice fulfilment (including nominating the employer's default fund) rates approaching 100%.

The additional compliance burden from stapling obligations has led to a considerable increase in the number of employers either using, or considering, onboarding software noting that cost of these

[2] Superannuation Guarantee (Administration) – Stapled Fund – Guidelines for the Reduction of an Employer's Individual Superannuation Guarantee Shortfall for Late Contributions Due to Non-acceptance by Notified Stapled Fund Determination 2021; and, Superannuation Guarantee (Administration) – Choice of Fund – Written Guidelines for the Reduction of an Increase in an Employer's Individual Superannuation Guarantee Shortfall Determination 2021.

solutions remains a primary barrier. ART supports options for employers that reduce compliance administration and increase efficiency at low or no cost and intends to participate directly in providing appropriate solutions to employers, as it did to help employers comply with SuperStream.

Whilst onboarding software assists employers to reduce the burden of stapling by capturing choice in larger volume, in circumstances where an employer is required to request a stapled fund, the initial Stapled Fund Request process is manual and inefficient. As highlighted by the Australian Institute of Superannuation Trustees (AIST) during YFYS consultation, the delay of a wholesale Stapled Fund Request solution prevented employers' onboarding service providers from integrating Stapled Fund Request within their platforms.

In our opinion, had a wholesale solution been provided to employers and their providers at stapling commencement, an increased number of employers would have taken up software solutions, leading to a reduction in the stapling compliance burden and a significant increase in stapling compliance compared to current levels.

How has the implementation of stapling changed onboarding, software and payroll processes for new employees?

As above, the implementation of stapling has increased the perceived need for and encouraged employers to take up onboarding software. For new employees, this has the effect of replacing paper forms and manual processes, with improved digital onboarding experiences. The mandatory nature of digital onboarding processes, and the improvement in fund choice experience, provides that more employees nominate a fund, whether that be their existing fund or their employers' default fund.

Anecdotally, where fund choice is not "mandated" by process, such as within digital onboarding, we have observed that employers are more strongly encouraging new employees to complete fund choice to reduce their onboarding administration. Whilst strongly encouraging new employees to nominate a fund may be perceived as positive, it may also have the effect of increasing pressure on an employee to make a quick or uninformed decision and can lead to the employees "choosing" the employers' default fund and the creation of a new account, in conflict with the intent of stapling.

15. Are there any barriers in the current framework to achieve the intent of the stapling reform?

As highlighted above, barriers to achieve the intent of stapling reform, that is to prevent creation of unintended multiple accounts when disengaged members change jobs, are:

- Low employer compliance due to associated administrative burden and/or cost of onboarding software solutions

The process to request a stapled fund from the ATO is manual and time consuming, adding to the existing compliance administration challenges faced by employers.

In contrast, software solutions that would reduce the burden of stapling compliance add an explicit, and oft times unachievable, cost to businesses. Software solutions are also not yet able to automate stapled fund requests due to the delay in wholesale solution to December 2022, which may result in a perceived lower value and uptake.

- Lack of perceived benefits (and associated delay in enforcement)

From an employer perspective, new employees are already provided the opportunity to nominate a super fund should they wish via existing choice processes and so new stapling obligations may represent for employers another example where responsibility, and therefore effort and cost, is transferred to the employer.

Many employers also carefully consider their employees' interests when selecting a default fund and so see the creation of an account within their default fund as a positive outcome, even where the employee has an existing super account. This is especially relevant where the employee is an existing member of a high fee or poorly performing fund.

Thus, in isolation, employers may not perceive stapling as beneficial. In the absence of any other benefit, an employer's reward for compliance with stapling takes the familiar form of avoiding penalties. Where enforcement is softened or postponed, there is limited justification for an employer to comply given the additional effort and/or costs.

16. What is the actual, or likely, impact of stapling on insurance coverage?

ART currently caters to multiple types of employer arrangements, each with unique insurance needs. A common element is the value that the different employer groups place on insurance in superannuation as an employee benefit.

Following the introduction of stapling, there is a risk that is still evolving that this benefit will be significantly lessened due to the availability of appropriate insurance.

Key elements of concern include:

- Impact on pricing due to reduced or altered insurance pools: insurance pools will change shape and demographic profile as fewer new members come into the pools. This could result in an older and potentially unhealthier cohort of members leading to increased pricing. As an employee benefit, some employers choose to subsidise insurance premiums for their employees. As these cohorts shrink due to new employees staying with a previous fund, employers will be less likely to provide this benefit to their employees.
- Impact on stapled individuals: If stapled to another pre-existing arrangement, there could be unintended insurance consequences for the individual. For example, they may miss out on valuable insurance cover provided under the arrangement which is unique to their employer. For example, a number of ART employers provides default Income Protection without underwriting. The cost of their insurance could also be materially different in the stapled arrangements versus the employer offer. Members who are stapled may not fully understand the need to make an informed choice about insurance coverage.

<u>Best financial interests duty</u>

17. To what extent has the BFID required trustees to change their processes and procedures? Has this caused any unintended consequences or impacted member outcomes in any way?

18. Are there certain types of expenditure or activity that trustees are particularly concerned about being able to prove compliance with the BFID in respect of? Why is it difficult to demonstrate compliance? Should there be a materiality threshold?

19. Is the reverse onus of proof the most appropriate way to achieve the objective of improving member outcomes?

ART acknowledges that the covenant placed on trustees to act in the best financial interests of members is a fundamental and core consideration in the decision making of a trustee. Indeed, this is aligned with the duty, that has always been placed on trustees, to act in the best interests of its members. As a trustee, ART agrees with the principle that a trustee should base its decisions on the best financial interests of its members and that the decision making process should have regard to relevant information for a decision of that nature. Trustees are required to make decisions today about the future, which is inherently uncertain. This requires judgement and expected outcomes can never be guaranteed. We are concerned that the reverse onus of proof creates uncertainty for trustees looking to make decisions for the benefit of its members into the future.

For example,

- There is a risk that innovation will not occur as undertaking new and innovative approaches or activities requires trustees to make a decision without past knowledge as to the outcomes of those proposed activities. Trustees may delay or refrain from dedicating funds to new innovations and longer-term strategic decisions. Over the long term, we consider that this will detriment members and is inconsistent with the long-term nature of superannuation;
- As a large national fund with members across a broad-spectrum of Australian communities, we recognise that many of our members have needs which are different to others and that there is a community expectation that ART will provide additional assistance and support to these members. For example, we consider activities that promote greater understanding of and access to superannuation (including in-person education services and additional online resources) provided to members in remote communities, vulnerable and disadvantaged members, and initiatives provided to support and promote financial literacy more generally among ART members are activities which are in members' best financial interests and contribute to creating better retirement outcomes for members. However, it is difficult to quantify the immediate and direct financial impact/benefits of education and support to the member from these initiatives and this creates uncertainty for the fund as to the documentation needed to support these activities;
- Currently the legislation does not provide for a materiality threshold, which creates uncertainty as to the requirements associated with expenditure of a small or essential nature. In administering the fund, there are certain activities that must be undertaken by a trustee. Further, many of those administrative activities result in the incursion of an expense that is of a small dollar value. Whilst trustees have processes in place to decide on the activities undertaken and expenses incurred, without a materiality threshold this creates uncertainty for funds as to the requirements associated with each expense (no matter how small or essential to the administration of the fund).

Noting the above examples, we are concerned that the reverse onus of proof and having no materiality threshold has created uncertainty as to a trustee's ability to make decisions for the benefit of its members into the future. Further, this uncertainty creates an additional burden (ultimately borne as administrative costs) as funds seek to respond to the unclear expectations as to documentary requirements associated with their decision making processes. In light of this uncertainty, we advocate for any future legislative amendments to remove the reverse onus of proof. This would allow trustees to confidently make decisions for the future benefit of its membership base. Clarification as to expectations could also occur by providing an express power for APRA, as the prudential regulator, to set standards prescribing expenditure and decision making requirements.