# 9 Maximising the benefits of the proposed reforms

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| Key points |
| * The Commission proposes that its reforms should ideally be legislated in full by 2014, so that the new process, together with the consideration of factors relevant to the selection of default products, can be applied in 2014. This could potentially occur in conjunction with the review of modern awards that will take place that year. * The reforms will affect stakeholders in different ways. * Employees who derive their default superannuation product in accordance with modern awards will benefit because their best interests will be the primary objective in the selection and ongoing assessment process, and there will be increased competition in the default market. However, some employees will find themselves in different funds, and will need to consolidate to avoid having multiple accounts. They will need accessible information from government agencies to help them make good decisions in response to the changes. * Employers generally will benefit from the improved administrative capabilities of the funds they deal with. However, some employers will incur the cost of changing default funds, and will need to be promptly informed of changes to award listings. * The reforms will not affect all superannuation funds in the same way. All funds that wish to have their default products listed in awards (including funds that are currently listed) will need to submit an application for listing in 2014, and at least every eight years thereafter. * The Default Superannuation Panel established within Fair Work Australia will have a range of responsibilities, and will need to be resourced appropriately. * From a community-wide perspective, the reforms should have the considerable net benefit of improving superannuation outcomes for employees who derive their default product in accordance with modern awards, and for fund members more broadly, by spurring improvement in the quality of superannuation products. * When superannuation products are listed in awards, their names and identification numbers need to be used in a clear and consistent manner, and a reasonable transition period will be needed, to allow employers and funds time to adjust. * An independent public review of the reforms should be conducted after the first periodic reassessment of all awards has been completed, ideally in 2023. It should examine whether the process and factors for consideration for default product selection remain useful and relevant, and include the possibility of employers being able to use any MySuper product as a default superannuation product. |
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This chapter examines the implementation and transition issues associated with the Commission’s recommended reforms to the system for listing default superannuation products in modern awards, with a view to maximising the net benefits of the reforms.

As discussed in chapter 8, the Commission expects that overall benefits will flow from the reforms it proposes. As is appropriate, the benefits will primarily be realised by employees who derive their default superannuation product in accordance with modern awards, and by members of default superannuation funds more broadly (by explicitly making the best interests of these employees the primary objective and by spurring improvement in the quality of default products). A range of benefits will also accrue to the wider community, as well as to some employers and superannuation funds.

The Commission’s proposed reforms will affect all stakeholders in the superannuation industry — employees, employers, funds and regulators, and will impose some costs. Costs of reform will be borne in particular by those funds (both listed and ‘grandfathered’) that are assessed as not meeting the best interests of employees who derive their default superannuation product in accordance with modern awards. They would no longer be able to receive default superannuation contributions made on behalf of those employees. Costs will also arise for the members and employers who were using those funds.

In order to fully realise the potential benefits of the reforms, the costs of implementation will need to be minimised to the greatest extent possible while still achieving the stated aims. The reforms should be implemented as soon as practicable (section 9.1) and employers promptly notified of the changes (section 9.2). Employees will need assistance to understand the changes and be encouraged to make informed decisions when required (section 9.3), and employers and funds will need a transition period (section 9.4). It is also essential that the Default Superannuation Panel be given appropriate resources and legal status (section 9.5) and that information about default products and their selection be made publicly available (section 9.6). Finally, the new process for selecting default products should be independently reviewed (section 9.7).

## 1 Implement the reforms as soon as practicable

### Participants’ views

Inquiry participants suggested a number of timeframes for implementing changes to the process used in the selection and ongoing assessment of default superannuation products for listing in modern awards. BT Financial Group (sub. 46), the Financial Planning Association of Australia (sub. DR76) and the Financial Services Council (sub. DR80) suggested that the introduction of the Commission’s proposed reforms could coincide with the introduction of MySuper products in 2013.

Similarly, the Australian Chamber of Commerce and Industry (ACCI) considered that:

… the requirement that default contributions from 1 October 2013 [now 1 January 2014] will need to be made into a fund authorized to offer a MySuper product, and that modern awards will only prescribe funds authorized to offer MySuper products has implications for the superannuation system … it is important that modern awards are varied sufficiently before 1 October 2013 to accurately prescribe post 1 October 2013 obligations. (sub. DR83, pp. 4–5)

In contrast, the Industry Super Network (ISN) suggested that:

… the process would be more effective if it was undertaken as a single exercise during the 2014 Fair Work Australia review of modern awards. The best means of achieving this, which may involve a staggered approach, should remain in the hands of the decision maker. (sub. DR62, p. 28)

Timing the proposed new default product selection process to coincide with Fair Work Australia’s (FWA) four yearly reviews of modern awards was also supported by DEEWR/Treasury (sub. DR89), and amounts to suggesting that the new process should not be implemented before 2014.

Others agreed with the view put forward by the Commission in the draft report, suggesting that assessment of the default funds listed in awards should occur as soon as practicable, and ideally during 2014 (for example, Business SA, sub. DR55; CSSA, sub. DR56). However, the Association of Financial Advisers considered that:

2014 is still a long way off … the current model is significantly deficient, and change is required as soon as possible. We believe that the Government should be capable of moving sooner than 2014 … (sub. DR73, p. 4).

Several others participants (including John McAuley, sub. 53; REI Super, sub. 26 and Tasplan, sub. 6) suggested that the implementation of the reforms should be delayed further — potentially by several more years. Unions NSW said:

There should be no change to the current default arrangements in awards until MySuper is fully bedded down and experienced. This in our view is 5 years. (sub. 13, p. 7)

ACCI took a different approach.

In ACCI’s view the assessment of funds for inclusion in an award should be driven by different considerations [to the award review process], the most important of which are the timing of Stronger Super and access to reliable data. The reality of both the Commission’s preferred options is that the normal processes applying to modern awards, including review and variation, will need to be modified for at least this aspect of their superannuation clauses to give effect to the policy object of the Commission’s preferred recommendations. (sub. DR83, p. 9)

### The Commission’s view

The Commission considered several potential timeframes for implementing the proposed new assessment and selection process set out in chapter 8. For instance, the introduction of the reforms could occur in 2013 to coincide with either:

* the initial introduction of MySuper products in July 2013
* the removal of funds that do not offer a MySuper product (or other approved default product) from awards, which must be undertaken by FWA by 31 December 2013.

However, in practice, the time required for the drafting and passage of relevant legislation (section 9.5) would preclude such rapid implementation. In addition, the Default Superannuation Panel needs to be selected and appointed, and a competent secretariat established.

A more realistic timeframe would be to implement the necessary legislative and policy changes during 2013 and 2014. Ideally, this would mean that the new process for listing default superannuation products in awards can commence during 2014. This approach has considerable merit.

* It would allow sufficient time to implement the necessary legislative and procedural reforms.
* It would minimise unnecessary delay.
* It would provide stakeholders with time to prepare for the changes. This will be particularly important for superannuation funds, given that the Commission recommends all funds seeking to have their products listed in modern awards will need to apply, including those funds currently listed in modern awards.
* It could potentially allow consideration of the superannuation provisions in awards to be undertaken in conjunction with FWA’s review of modern awards, thereby minimising the overall cost of undertaking the award variations that will be required. (The review of modern awards is prescribed by section 156 of the *Fair Work Act 2009* (Cwlth) and is scheduled to take place early in 2014.)

While delaying the reforms for several more years would have the benefit of allowing the industry to fully adapt to the MySuper reforms before starting additional reforms, it unnecessarily postpones realisation of the benefits of the reforms.

In recommending that the new selection process for default products should, if possible, be applied in 2014, the Commission does not intend to limit the Default Superannuation Panel’s scope to stagger consideration of the products listed in default awards, or to consider groups of awards at the same time (chapter 8).

Recommendation 1

The legislative and policy changes necessary to give effect to the Commission’s recommended reforms should ideally be put in place in 2013 and 2014. This would allow the new process, together with the consideration of factors relevant to the selection and ongoing assessment of default superannuation products for listing in modern awards, to be applied during 2014, and potentially coincide with the review of modern awards that will take place that year.

## 2 Promptly inform affected employers

### Participants’ views

Several participants emphasised the importance of notifying employers when a fund can longer accept default superannuation contributions for employees who derive their default superannuation product in accordance with modern awards.

Employers would need to firstly be made aware that the fund is non-compliant, consult with employees over a new fund, invest time, money and resources into adjusting superannuation payments to funds that do meet the stated criteria and adjust relevant electronic financial transactions. We suggest that if existing funds are found to fail the new criteria, the government must provide for:

* … A notification to both employers and employees concerning the status of their current fund in relation to compliance.
* A 12 month transitional period whereby employers have time to identify a new default fund. (Electrical Contractors Association, sub. 17, p. 2)

Business SA considered that:

As the new default superannuation fund process is implemented, it will be necessary to inform and educate businesses [about] the system and what their options are. This should be conducted by [the Australian Prudential Regulation Authority (APRA)] in association with business membership organisations. (sub. DR55, p. 3)

### The Commission’s view

When a fund is no longer permitted to receive superannuation contributions made on behalf of employees who derive their default superannuation product in accordance with modern awards, notifying employers who are contributing to these funds on behalf of these employees is the first and most crucial step in ensuring that contributions begin to flow into the products and funds listed in the award. Indeed, employers are the only participants in the superannuation system who are aware of precisely which employees derive their default superannuation product in accordance with modern awards.

* Employees will not necessarily know whether they are award reliant, or which award applies to them, or of the role the award plays in determining the destination of their superannuation.
* Neither superannuation funds nor government agencies have sufficient information about the employment arrangements of individual employees that could be used to identify and notify all employees who derive their default superannuation product in accordance with modern awards.
* Employers are required to provide employees with the entitlements specified in the award or agreement, and to keep records when employees exercise choice of superannuation fund. This means they should know which employees derive their default superannuation product in accordance with modern awards and which are in the default superannuation fund.

Few data that would enable employers to be identified and contacted are available. The Australian Taxation Office (ATO) enforces superannuation guarantee requirements, and in so doing collects information, for its own use, about employers and the superannuation contributions they make. The Australian Securities and Investments Commission has a register of business names, but access to many of the details in the register is limited and, importantly, many businesses do not employ staff.

This means that no data are publicly available that would enable the employers of workers who derive their default superannuation product in accordance with modern awards to be identified (which is a necessary first step in contacting them to advise them of the changes). Therefore, in attempting to ensure that all affected employers are notified of changes to award default superannuation arrangements, it will be necessary to use a number of channels. Employers could be contacted and provided with relevant information through:

* the ATO
* industry-specific, state and national employer organisations (though some employers may not belong to any of these types of organisation)
* FWA’s award-specific electronic mailing list (though many employers may not subscribe to these lists)
* notices and articles in mainstream and industry-specific media.

This may result in some employers being informed of the changes to award default fund listing more than once, and in others not receiving any direct notification. This situation also arises when other aspects of awards — notably wage rates — are changed. Employers may (or may not) be notified of changes to award wages through one of the channels listed above, but are nevertheless expected to pay current wage rates. To the extent that employers are able to keep abreast of award wage requirements, similar systems should prove sufficient for notifying employers of changes to award default superannuation arrangements.

## 9.3 Assist affected employees to understand the changes and make informed decisions

### Participants’ views

A number of inquiry participants commented on mechanisms for, and the importance of, notifying employees of changes to award default superannuation arrangements. ISN considered that:

… it would be reasonable to have processes in place that inform any employees who are members of the fund that the fund, although remaining MySuper authorised, is no longer listed in the relevant award and informing the employee that choice is available to them and that they should in the circumstances seek independent financial advice. (sub. DR62, p. 25)

ACCI described how employees might respond when they are notified that the default fund has changed.

Some employees might decide to choose the former fund, perhaps because the employee has selected an investment option with that fund. Some employees might decide to exercise choice, and nominate a totally different fund, perhaps because they do not like the proposed new default. There is no particular time by which an employee must return a choice form. Under the current regime employees not choosing the former default fund would end up with an additional account, although the implications of this may be reduced under SuperStream. (sub. 37, pp. 5–6)

AiGroup commented on the burden that changing funds would place on employees.

Asking employees to become accustomed to a new fund, to provide a new fund with information already provided to their existing fund, to reassess insurance offerings and other features of the new fund and to re-nominate their beneficiaries in the event of the employee’s death, would impose a burden upon employees. (sub. DR79, p. 5)

Mercer sounded a note of caution about:

… significant disruptions and cost for … employees who are members of the delisted fund and who may end up with two accounts (and two sets of fees and insurance premiums) and/or incur a withdrawal fee when their existing account is transferred to their new fund. (sub. DR68, p. 3)

The Law Council of Australia warned of the:

… potential for employees to suffer loss if their superannuation is unilaterally moved to new default funds from current default funds in which they have been members for many years. This may have a significant effect on employees’ insurance cover, and may give rise to additional fees and charges payable by employees who acquire multiple accounts. (sub. DR67, p. 5)

Rural and Regional Promotions highlighted that:

… many members in default funds are unaware that they have the ability to switch from one fund to another, this also adds to their disconnect from taking an active interest in their fund. There is a natural disinclination for funds, unions and employers to actively advise members that they are free to switch to other funds. (sub. DR86, p. 3)

### The Commission’s view

As discussed in previous chapters, the proposed reforms are designed primarily to benefit employees who derive their default superannuation product in accordance with modern awards. The proposals aim to ensure that employees who are placed into a default fund listed in an award will have their best interests served by that placement. The reforms are likely to also benefit employees who choose one of the products listed in an award.

The proposed reforms will be clearly beneficial for employees who are entering the labour market for the first time and who do not exercise their right to choose a fund, as there will be a greater chance that these employees become members of a fund that meets their best interests.

In addition to benefiting new employees, the proposed reforms will also benefit existing employees who are moved to a fund that in net terms better meets their interests. It is, however, difficult to estimate how many employees will change funds as a result of the reforms (box 9.1). As discussed in chapter 8, the overall effect on these employees is likely to depend on whether they consolidate their superannuation balances into the new product and fund, the savings they make in terms of reducing the number and value of administration fees and insurance premiums they are charged, and the effect that the consolidation may have on their insurance coverage.

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| Box 9.1 Estimating the number of employees who will change funds as a result of the proposed reforms |
| The number of employees who have their contributions paid to different funds as a result of the reform to the selection process for default superannuation products in modern awards will depend on a range of factors. These include:   * the number of funds that are currently receiving default contributions but do not have products listed in awards once the new selection process has taken place. These funds include: * those that are currently listed in a modern award but do not obtain listing for their default product(s) following the new selection process * those that were receiving contributions under the 12 September 2008 grandfathering clause, and do not obtain listing for their product(s) following the new selection process. * the rate of uptake of enterprise agreements (which can provide for default contributions to be made to funds that are not listed in the award) * whether employees exercise choice of fund in the face of a proposed fund change, in favour of their current fund or another fund.   The number of employees who exercise choice of fund will in turn depend on employees’ awareness of their current superannuation arrangements, their satisfaction with those arrangements, and their willingness to incur the costs of changing funds in order to derive the benefits of moving into a fund that better suits their needs. These costs could include exit fees; the time and effort involved in assessing options, making decisions and completing paperwork; and the risk that the chosen fund proves to be a relatively poor choice for that employee (chapter 3). |
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There are also several other potential ways in which employees (and fund members more generally) may be affected.

* To the extent that funds that no longer have products listed in awards experience a decline in investment returns (see below), this decline is likely to flow through to the returns to remaining fund members
* Superannuation funds will incur some additional costs in applying to list their default products in modern awards, and may pass those costs on to members.

Given the potential for employees to be made worse off by paying multiple fees and insurance premiums — even when their future superannuation contributions are made to a product that has been assessed as being a better choice — it is important to ensure that affected employees have enough information to make informed decisions about their superannuation, and particularly about account consolidation and the insurance implications of changing funds.

#### Current and planned mechanisms for informing and assisting affected employees

Ensuring that affected employees have sufficient information to make informed decisions about their superannuation will, at a minimum, involve:

* informing employees that their superannuation contributions will be paid to a different fund if they don’t make an active choice, and which product will receive their future contributions by default
* reminding them that they are free to choose any product offered by any fund that will accept them as a member, including those not listed in the award
* providing information which explains how to consolidate multiple accounts, and the potential benefits and costs of doing so.

As discussed in section 9.2, employers will take a primary role in informing employees who derive their default superannuation product in accordance with modern awards that default superannuation arrangements have changed. Employers are currently required to use the ATO’s standard choice form to notify employees that the employer is changing default funds. The standard choice form includes the name and contact details of the new fund. The instructions for completing the form strongly encourage employees to read ASIC’s consumer guide to superannuation (box 9.2).

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| Box 9.2 *Super Decisions* |
| *Super Decisions* is a free consumer information booklet prepared by the Australian Securities and Investments Commission. It explains the basics of superannuation and provides guidance on super choice and how to compare funds.  It provides ‘key tips about super’ that are expressed in simple, everyday language:  Look before you leap when choosing a fund. Compare retirement and insurance benefits and other features. Keep fees and charges down.  Super’s a long term investment, so take investment ups and downs in your stride.  Consolidate your super accounts where possible, to avoid paying fees for more than one account and to stop you losing track of your super. Keep your fund(s) up to date with your address and how you’d like your death benefits paid.  If you’re changing or consolidating super funds, make sure you don’t lose valuable insurance benefits. (p. 4) |
| *Source*: ASIC (2011b). |
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The new superannuation fund will also provide information to affected employees, in the form of a product disclosure statement. This must be distributed within three months of the new member joining the fund. From 1 July 2013, funds will also be required to report contributions to their members on a quarterly or six-monthly basis. This is designed to ensure that employees can track whether their superannuation entitlements are paid in a timely manner, and may further assist in raising members’ awareness of, and engagement with, their superannuation.

In addition, the potential for multiple small account holdings to persist will be partially mitigated by the introduction of account auto‑consolidation (box 9.3).

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| Box 9.3 Auto-consolidation of accounts with low balances |
| The Government has announced a program of auto-consolidation for superannuation accounts with low balances.  From January 2014, the ATO will facilitate the auto consolidation of accounts with low balances by providing details of these accounts to members’ active funds. The information will be provided annually and will include details of lost accounts, accounts that have not received a contribution or rollover for two years with balances under $1,000 and accounts in eligible rollover funds. These are the accounts that the government has identified as candidates for auto consolidation. Funds will be responsible for arranging consolidation unless the member opts out. (ATO 2012d)  The aim of auto-consolidation is to ‘reduce the amount of fees paid on multiple accounts and maximise retirement benefits’ (Shorten 2011a). As such:  The $1,000 auto consolidation threshold may increase to a higher amount subject to a review by the Treasury, ATO and [the Australian Prudential Regulation Authority] in late 2014. (ATO 2012d)  The importance of auto-consolidation is recognised by the industry.  The value of these initiatives to counter the problem of many people holding multiple accounts, often with small balances, and seeing their savings eroded through the payment of multiple administration fees and insurance premiums, is widely endorsed. The need to ensure that members clearly understand the impact of a move to consolidate their accounts, including on their insured position, was often emphasised during discussions as was ensuring that there is a genuine ability for a member to opt-out of this process if they determined that it was in their interests to operate multiple accounts. (Australian Government 2011b, p. vii)  Changes to legislation and regulations to give effect to auto‑consolidation are yet to be drafted, and so some details (such as the timeframes in which funds must consolidate accounts and the treatment of accounts with active insurance policies) are not yet known. |
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#### Are further measures to assist employees required?

The combination of notification via the standard choice form, general advice in the *Super Decisions* publication, product disclosure from the new superannuation fund and auto-consolidation of accounts with low balances will ensure that all affected employees are informed of the changes to their superannuation arrangements and will have access to information to help them decide whether to consolidate multiple superannuation accounts (or for funds to undertake that task for them in certain cases).

Despite these measures, it is possible that having future superannuation contributions paid into a different fund will be disadvantageous for some employees who derive their default superannuation product in accordance with modern awards. Adverse effects are most likely to arise where the change of fund leads to multiple account holdings and members do not consolidate their accounts (which they are able to do at any time). Even when consumer-friendly information is available, ‘many consumers remain ignorant of why account consolidation is important or how to go about it’ (Choice 2006, p. 15). It can also be difficult for consumers to understand the ways in which account consolidation could affect their insurance coverage.

The program of auto-consolidation for superannuation accounts with low balances (box 9.3) provides a partial response to this inertia. A similar system of auto‑consolidation could potentially be established for accounts with higher balances, where the multiple accounts have arisen due to changes to default superannuation arrangements in awards. However, in considering such an approach a number of significant issues arise.

* First, there is no way of reliably distinguishing between employees who have never made decisions about their superannuation (and so are truly in the default fund by default), and those who have actively chosen to be in a fund that is their employer’s default fund (but who have not filled in a choice form to that effect, or did so more than five years ago). An auto-consolidation program is therefore likely to include many employees who have chosen to be in their current product or fund. While those employees could opt out of the auto‑consolidation, the existence of a significant number of employees who wished to opt out would negate many of the benefits of automating consolidation in the first place.
* Second, it is likely that auto-consolidation would result in some employees losing valuable insurance coverage. As discussed in box 8.6 (chapter 8), it is possible that the new fund may exclude coverage for certain events, occupational hazards or pre-existing medical conditions that were covered by the old fund. In such situations, employees are likely to benefit from retaining insurance policies offered by the old fund, and would be adversely affected if their account was automatically consolidated into the new fund. Though some employees will be aware of these insurance issues and opt out of auto-consolidation on that basis, it is possible that many of the default members who would have been better off retaining their current insurance coverage would not take the steps needed to do so.
* Third, the number of employees who will be affected by the changes to award default arrangements is not yet known (box 9.1). Were a large number of employees to be affected and their balances automatically consolidated to their new funds, there is potential to significantly adversely affect the stability of, and thus the returns received by members (including choice members) in, the old funds. Depending on the size of the funds that were no longer able to receive contributions for employees who derive their default superannuation product in accordance with modern awards, the movement of these employees from these funds could in turn have implications for the stability of the superannuation market, and the confidence people have in it.

In light of these issues, the Commission does not consider that auto‑consolidation of multiple accounts that have arisen due to changes to award default arrangements would be appropriate at this time. Measures outlined in chapter 8 to minimise the transitional effects on members mean that fewer employees are likely to have multiple accounts, and thus the potential benefits of auto-consolidation are commensurately smaller.

## 9.4 Allow a reasonable transition period for employers and funds

Many employers and superannuation funds will be affected by the changes to award default superannuation arrangements. To a large extent, these effects will be transitional in nature. As such, the provision of an adequate timeframe for transition will be important in minimising any potential adverse consequences of the reforms.

### Participants’ views

#### Consequences for employers

A number of inquiry participants (including the South Australian Wine Industry Association, sub. DR71) commented on the potential consequences of reforms to the default system for employers, particularly if the reforms require them to change default funds.

REST Industry Super said that:

… there is no question that changes to the nominated default superannuation fund would cause some inconvenience, be it the need for system configuration, the use of disclosure material to employees and associated material to all recruitment locations, as well as the need to liaise with additional parties for contribution reconciliations and insurance claims. (sub. 47, p. 10)

ACCI commented:

When an employer changes the fund into which default fund contributions are being made the employer must give the affected employees (employees who have not chosen a fund whose contributions are being paid into the former default fund) a new standard choice form which identifies the new default fund. The employer may have to enter into a standard employer sponsorship with the new default [fund] unless there is already such an arrangement in place. The employer will have to enrol all affected employees except those who return a properly completed standard [choice] form before that happens. (sub. 37, p. 5)

AMP suggested that:

The administrative burden placed on employers, especially medium to large employers, in changing default superannuation funds is also considerable. In order to change a default superannuation fund, an employer is bound by the Superannuation Guarantee Act to issue all employees with a choice of fund form (and act on and retain returned forms). (sub. DR85, p. 7)

Mercer warned of ‘significant disruption and costs for many thousands of employers’ (sub. DR68, p. 3).

Similarly, AiGroup said:

Changing default funds would impose a substantial compliance burden on employers. In addition to changes in payment arrangements and the like, it would also require an employer to identify which employees had chosen to contribute to funds previously listed in an award and which employees were members of these funds as a result of their being listed as default funds. (sub. DR79, p. 5)

The Association of Superannuation Funds of Australia (ASFA) suggested that if employers are not required to change from their existing default fund, they may be unlikely to do so.

Incumbency is also very important for determining which fund or funds are being used as a default. Changes to default funds listed in an award (in terms of any additional fund or funds being listed) are unlikely to lead to many employers reconsidering the default fund they use. (sub. 31, p. 6)

#### Consequences for superannuation funds

Several inquiry participants put forward views on the potential consequences for superannuation funds of any reforms that led to different funds receiving contributions made on behalf of employees who derive their default superannuation product in accordance with modern awards.

REST Industry Super said that:

… if a fund loses membership through the opening up of default fund status in modern awards, this could impact on its ability to continue to offer the benefits of scale to its members … Loss of [funds under management] results in higher cash outflows and increases the need for liquidity in the fund’s default investment option. This could limit the ability of a fund to invest in less liquid assets such as infrastructure projects which typically are expected to provide higher returns than other assets classes but are illiquid and require significant capital investment … The removal of infrastructure based on the assumptions outlined above results in reduced gross returns. (sub. 47, pp. 11–‍13)

Mercer similarly warned of:

… a potentially disastrous impact on the delisted fund (with a potential large call on its assets as members transfer account balances to the new default funds of the thousands of employers who can no longer contribute to the fund) and a significant drop in contribution inflows. The fund’s liquidity and future investment returns may also be adversely impacted. (sub. DR68, p. 3)

Mercer also considered that removing a fund from award listing could result in ‘a potentially serious adverse impact on the remaining members of the delisted fund with its reduced scale, potential fee increases and potential lower liquidity’ (sub. DR68, p. 3).

Likewise, ACCI suggested that:

In the world of MySuper defaults there will be a clear competitive advantage for a fund to be nominated in one or more modern awards and it seems likely that funds offering MySuper products which fail to be nominated in any relevant modern award will seek to amalgamate or perhaps to exit the default field. (sub. DR83, p. 5)

MLC Ltd–NAB Wealth suggested that ‘forced transition of superannuation arrangements (to specifically named funds in awards)’ will involve ‘significant adverse consequences (for members)’ (sub. DR87, p. 6).

… moving members from their current option on a single prescribed day or in a short time frame will expose members to transactions undertaken without regard to their investment merit (i.e. potentially selling low, buying high) …

Funds and products within funds have commonly had illiquid assets (with an appropriate calibration to expected entrants and exits). These can be classified either as assets that are illiquid due to the characteristics of the underlying investments (property or private equity for example) or assets that are illiquid due to legal impediment. In both cases the valuation of the asset can be problematic and if it is to be moved into a new fund structure it needs to be quarantined to ensure that it does not affect the investments of other clients or members. Some funds may not have the capacity to manage and/or quarantine these assets …

Of particular concern would be the consequences of large sums moving around the industry over short periods of time. The potential for arbitrage in the market place at an industry wide level could be huge, to the detriment of the uninformed member. (sub. DR87, p. 6)

#### Transition period

AIST (sub. DR69), the Electrical Contractors Association (sub. DR84) and the South Australian Wine Industry Association (sub. DR71) suggested that a transitional period of at least 12 months should be provided, ‘so that employers can get advice regarding their default fund and communicate the change to employees’ (sub. DR71, p. 4).

Mercer recommended that:

… employers be provided with a three year period to justify their default is appropriate … Any shorter period may hinder the ability of employers to make an appropriate choice of default fund (sub. DR68, pp. 3 & 10)

### The Commission’s view

#### Consequences for employers

For those employers who are affected by the reforms, there will be ongoing benefits for some, and additional costs for others, albeit generally of a transitional nature. Employers will be particularly affected by the Commission’s proposed reforms if they were making contributions to a fund that is no longer able to receive contributions made on behalf of employees who derive their default superannuation product in accordance with modern awards. Those employers will be required to change to one of the funds that offers a default product that is listed in the award.

As noted above, these employers will be required to use the ATO’s standard choice form to notify employees that the employer is changing default funds. If the standard choice form is provided to all employees who are currently members of the default fund, employers will satisfy their requirements, obviating the need for them to search their records to ascertain how employees came to be in that fund.

The number of employers who change funds as a result of the reforms will depend on a range of factors that mirror those affecting employees outlined in box 9.1. As participants highlighted, changing default superannuation funds would involve a range of (largely transitional) administrative costs. Given that there will be between four and eight years between wholesale reassessments, these transitional costs would occur infrequently for the vast majority of employers (and many employers will not incur them at all, because they will continue to be able to use their current default fund).

Indeed, in some cases, a change of default fund could bring ongoing benefits to employers, if it means that they are able to select a fund that has better administrative systems or is more efficient in responding to their needs. In this regard, one of the factors for consideration in the selection and ongoing assessment of funds is its administrative efficiency (chapter 6). The Commission anticipates that the greater competition between funds will improve this aspect of their operation (amongst others), to the benefit of all employers. In addition, there will be direct benefits to employers who are newly able to engage with a longer list of funds that have better administrative capabilities.

#### Consequences for superannuation funds

##### Funds that can no longer receive award default contributions

As noted above, some of the costs of reform will be borne by funds that are no longer able to receive contributions made on behalf of employees who derive their default superannuation product in accordance with modern awards. Until the Commission’s proposed new selection process is completed, it is not possible to know exactly which funds these will be (or how many such funds there will be). However, it is clear that this group will include:

* funds that are currently listed in a modern award and that are not successful in having their default product(s) listed following the Commission’s proposed new selection process
* funds that were receiving contributions under the 12 September 2008 grandfathering clause, and that do not obtain listing for their default product(s) following the new selection process.

Similar considerations will also apply for funds with products that are listed following the new selection process, but are later found not to sufficiently meet the factors for consideration and are removed from award listing.

The affected funds may experience a reduction in membership and funds under management. They may also lose any reputational benefits that being listed in an award may bring. With less certainty about future income, they would need to adjust their investment portfolios. They may simultaneously be adjusting their portfolios in response to heightened incentives to improve investment performance (chapter 7).

However, the only funds that will experience these reduced returns are those that offer a default product that does not meet the requirements of the new process — that is, funds whose default product has been judged as delivering outcomes that are unsuited to employees who derive their default superannuation product in accordance with modern awards. As such, the Commission considers that these funds were advantaged by having previously been listed as default funds in awards, rather than disadvantaged by no longer being listed. Moreover, given the dynamic nature of the superannuation industry, the funds that are no longer able to receive award default contributions can work to have their products relisted by better addressing the factors for consideration. Funds also have the option of directly approaching employers and employees to obtain default status at the enterprise level through an enterprise agreement, or to become the fund of choice for individual employees.

##### Other consequences for funds

Most funds will also be affected because they will face greater competition in the default market. This will particularly affect the funds that are included in those modern awards that currently list only a handful of funds (chapter 7).

In addition, any fund that wishes to have its default product listed in a modern award will bear the costs of participating in the application and selection process in 2014 and every four to eight years thereafter. At a minimum, this will require every fund that wishes to have its default product listed (including funds that are already listed) to articulate their claims for selection against the factors for consideration recommended by the Commission. Funds that are not successful in obtaining inclusion will bear this cost for no return.

#### Transition period

The Commission is mindful that employers will need to be given a reasonable period of time to make necessary changes once new default products are listed in any award. Likewise, superannuation funds will need time to adjust their investment portfolios in response to changes in the projected flow of funds. This suggests that providing an adequate timeframe for transition will be important for both employers and funds.

The Minimum Wage Panel within FWA — on which aspects of the Default Superannuation Panel are modelled — provides a short transition period for annual changes to award wages. In recent years, the panel has announced its decision in June, with the new wage rates taking effect on 1 July. A similar mechanism, but with a significantly longer adjustment period, could be used by the Default Superannuation Panel.

FWA has used a range of other transition periods during award modernisation and for other variations to award provisions. Some award variations apply from the date of the decision, some are backdated, some apply on a fixed date in the near future, and others are gradually phased in over a number of years. These different responses depend on the time needed by stakeholders (notably employers) to adapt to the changes, and the risk of adverse consequences that could arise if changes were made too quickly.

The Default Superannuation Panel will be best placed to assess these risks, and to determine whether, and the extent to which, they vary between awards. The Commission therefore considers that when listing default products in awards the Default Superannuation Panel should also decide on appropriate transition periods. In doing so, it should take into account the best interests of employees who derive their default superannuation product in accordance with modern awards, as well as the needs of employers and superannuation funds. Providing a reasonable transition period will also assist in mitigating any wider risks to the superannuation market that may arise during transition.

## **9.5 Ensure that the Default Superannuation Panel has appropriate skills, resources and legal status**

Participants expressed a range of views about whether the Default Superannuation Panel within FWA would be an appropriate decision maker, and about whether it would possess, or could acquire, the necessary skills and experience to make decisions in the best interests of employees who derive their default superannuation product in accordance with modern awards. These views are addressed in chapter 8.

#### **Resources for the Default Superannuation Panel**

The Default Superannuation Panel (supported by a secretariat) will need to perform a range of new functions. These include:

* calling for applications from superannuation funds that wish have their default products listed in modern awards, and for information on the needs and best interests of employees who derive their default superannuation product in accordance with modern awards
* considering the information provided by superannuation funds, industrial parties and other interested stakeholders
* exercising judgement about how the applicant products and funds compare against each of the factors for consideration recommended by the Commission (and potentially other factors) for each award or group of awards
* selecting suitable products for listing in each award or group of awards, and a small subset of funds to be identified as best meeting the interests of employees who derive their default superannuation product in accordance with modern awards
* publishing applications, decisions (and potentially draft decisions) and other relevant information
* maintaining an awareness of the suitability of listed products for employees who derive their default superannuation product in accordance with modern awards, through an ongoing assessment process, including ongoing liaison with APRA
* conducting a wholesale reassessment of the list of funds every four to eight years
* undertaking associated administrative tasks.

FWA will require additional resourcing to allow the Default Superannuation Panel to successfully fulfil these functions. The level of resourcing will need to be sufficient for it to obtain the necessary expertise to conduct these new tasks. The exact level of resourcing needed to accomplish this will depend on the detail of the processes adopted by FWA, and on the existing resourcing and expertise that it can bring to this task.

By way of indicative guidance, the budget papers prepared for the former Australian Fair Pay Commission (the predecessor of the Minimum Wage Panel) show that its budget was close to $7.5 million in 2008-09 (O’Neill 2009). FWA does not disclose the full resources currently employed by the Minimum Wage Panel.

It will be important that the panel’s budget is clearly separated from the budget allocations used for FWA’s other functions. Such quarantining will ensure that the process is transparent and provides a basis for assuring all stakeholders that the selection of default products for listing in modern awards is conducted in an appropriately rigorous fashion.

Resourcing will also need to be sufficient to enable the Default Superannuation Panel to obtain relevant data in a timely manner. This may be particularly important given the limited availability of data on employees who derive their default superannuation product in accordance with modern awards (box 9.4).

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| Box 9.4 Data on employees who derive their default superannuation product in accordance with modern awards |
| The Default Superannuation Panel’s decisions will affect employees who derive their default superannuation product in accordance with modern awards. As discussed in chapter 2, this includes:   * award-reliant employees * employees who receive above-award wages but are reliant on the award for their superannuation, and * employees covered by enterprise agreements that incorporate the superannuation provisions in the award by reference.   However, there are currently no award-level data on any of these groups, and thus there is no precise measure of the number of employees who derive their default superannuation product in accordance with modern awards. This absence of data makes it difficult to estimate the number of employees who will have their contributions paid to different funds as a result of the reform to the selection process for default superannuation products in modern awards (box 9.1).  Fair Work Australia is currently mapping the coverage of each modern award to the industry classifications used by the Australian Bureau of Statistics. Drafts of this work were published in August 2012 (FWA 2012c). Once completed, these maps should assist in obtaining data on award-reliant employees.  There may then be scope for further work to refine the identification of award-reliant employees and improve the data collected on superannuation provisions in individual and collective agreements. However, the feasibility of obtaining reliable data, and the costs and benefits of their collection, would need to be carefully assessed. |
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### Legal basis and protections

#### Participants’ views

The Law Council of Australia commented on a number of legal issues of relevance to the operation of the Default Superannuation Panel.

Consideration also needs to be given to the possibility of:

(i) a fund seeking judicial review of the decision; and

(ii) exposure to legal actions (in the form of individual or class actions) for compensation to:

(A) a fund that is excluded from an approved ‘default MySuper’ list as a result of an error made in the assessment process;

(B) a fund that has suffered a loss as a result of something published by FWA or the expert panel that is incorrect; or

(C) employers or employees for loss suffered as a result of contributing to MySuper products selected by FWA or the expert panel on its approved ‘default MySuper’ product list.

… Consideration needs to be given to the legislation that would need to be put in place to ensure that FWA or the expert panel applies the criteria for its approved ‘default MySuper’ product list consistently with other Commonwealth legislation (ie. the Corporations Act 2001 (Cth) and the Future of Financial Advice (FOFA) legislation). (sub. DR67, pp. 4–5)

#### The Commission’s view

The Default Superannuation Panel will need a legislative basis for its operations. The Commission envisages that this could be partly modelled on current legislative arrangements for the Minimum Wage Panel that are contained within the *Fair Work Act 2009* (Cwlth). In developing the legislative framework, it will be important that:

* the factors for consideration are prescribed in the legislation (recommendation 7.1)
* principles of good process (recommendation 7.2) are followed
* all aspects of the default product selection process (as recommended in chapter 8) are provided for in (or permitted by) legislation, including that all eligible superannuation funds have standing solely for the purpose of listing default superannuation products in modern awards
* a legislative basis is provided to enable APRA to share data with the Default Superannuation Panel, and vice versa.

Inquiry participants raised a number of concerns about legal consequences that could arise from the Default Superannuation Panel’s decisions in certain situations, such as very poor performance of a listed superannuation product, breach of statutory duty or negligence. As a consequence of participants’ concerns, the Commission obtained legal advice from the Australian Government Solicitor (AGS) about whether a Default Superannuation Panel could be liable in such situations. The AGS advised that if the panel was established under the Fair Work Act, section 580 of the Act would protect members of the panel from liability. This would not, however, prevent the decisions of the Default Superannuation Panel from being reviewed by the judiciary for jurisdictional error (decisions made by FWA and the Minimum Wage Panel are similarly reviewable). The Commission seeks to limit opportunities for appeal in order to avoid vexatious claims but supports the provision of review where the panel has not properly exercised its jurisdiction (chapter 8).

## 6 Provide clear information about default products and their selection

### Public reporting

A recurring theme of this report is that, for the best interests of employees who derive their default superannuation product in accordance with modern awards to be fully realised, an open and transparent process is needed to assess which products should be listed as defaults in modern awards. This openness and transparency must extend to all aspects of the decision-making process.

#### Participants’ views

Of all the inquiry participants, Suncorp made the most detailed suggestions about openness and transparency.

Suncorp suggests that FWA should be required to publish an annual report into the default superannuation in modern awards system. Key statistics that should be included in the report are the:

* number of applications received
* number of applications approved or denied
* reasons for denial
* average time taken to assess applications
* longest time taken to assess an application
* estimated number of employees working under awards that had applications denied
* estimated annual dollar value of superannuation contributions made under awards that had applications denied
* number of awards reviewed and not reviewed for default superannuation fund purposes.

In all cases these statistics should be provided both in total and broken down by fund type. (sub. 38, p. 6)

#### The Commission’s view

The Commission considers that Suncorp’s suggestions have merit, though the capacity for reporting to occur on an annual basis will depend on the choices made by the Default Superannuation Panel about the conduct of the selection process. Unless some form of staggered or rolling assessment is adopted, periodic reporting timed to coincide with the four to eight yearly reassessment process may be more appropriate.

In terms of publishing information about the process used to select default products, the most useful information to report and the most appropriate reporting formats will depend on a range of factors that are best assessed by those with day-to-day involvement in the process. Accordingly, the Commission does not intend to specify in detail exactly how the Default Superannuation Panel should report on the process it uses to select superannuation products for listing in awards. It is already FWA’s practice to publish a statement of its decisions, and the Default Superannuation Panel would be required to adopt a similar practice.

### Clearly identifying products in awards

There is currently considerable variation in the way in which default superannuation funds are listed in modern awards. For example, Asset Super is listed in different awards as either Asset Super, Asset Limited or the Australian Superannuation Savings Employment Trust. In addition, some funds named in awards no longer appear to be operating.

Although the 122 awards name 103 funds the number of active funds has been reduced to approximately 86, with 6 funds wound up; 7 funds merged and the status of 4 funds is unknown but not active. A number of funds do not exist as named in awards. (ISN, sub. 27, p. 36)

The variation in fund names and the presence of non-operational funds in awards can make it difficult for employers to be confident that they have correctly identified the funds to which they are required to contribute.

The Commission’s reforms provide an opportunity to rationalise the way in which default products are listed in awards. In the draft report, the Commission recommended that the superannuation fund names and identifying numbers used by APRA should be used by FWA to list superannuation funds in modern awards. Since the draft, for reasons discussed in chapter 7, the Commission has formed the view that default superannuation products should be assessed by the Default Superannuation Panel. As a consequence, default superannuation products, rather than funds, should be listed in awards.

However, while each MySuper product will have a generic name, funds will also be able to give the product different names when offered to members from a particular subset of the total membership of that product — a practice known as ‘white labelling’. Though the white labelled products will have the same investment strategy and the same fee structure, they will be permitted to have different names, logos and member communication material, including different product disclosure statements (APRA 2012c). In order to prevent confusion about white labelled products on the part of both employers and employees, it will be important to ensure that, in addition to the generic product name, the fund name and product identifiers are listed in awards.

Recommendation 2

The product names and identifiers and fund names used by the Australian Prudential Regulation Authority should be used by Fair Work Australia to list default superannuation products in modern awards.

As mentioned in chapter 8, draft legislation currently before Parliament provides that if APRA cancels the authorisation of a fund to offer a MySuper product, it must notify FWA in writing of that fact (Shorten 2012a). The Commission supports this approach, and considers it to be an essential feature of a well-functioning award default system.

### Other issues that may require special consideration

#### Exempt public sector superannuation schemes

Exempt public sector superannuation schemes (EPSSSs) will not be able to offer MySuper products, but will nevertheless be eligible for selection as a default fund in a modern award. Some of the recommended factors for consideration could have a different degree of importance in relation to EPSSSs. Comparing default products offered by EPSSSs with MySuper products on an equal basis may also pose challenges, as EPSSSs are not bound by the same regulatory framework. They may structure their default products in different ways, and may collect and report different information to other funds. Therefore, the Default Superannuation Panel will need to be aware of the impact that its processes may have on EPSSSs, and ensure that it does not place an undue burden on them. The panel should nevertheless strive to assess EPSSSs on the same basis as they do other funds.

#### Modern enterprise awards

The Fair Work (Transitional Provisions and Consequential Amendments) Act 2009 (Cwlth) provides that a range of existing awards that apply to a single enterprise may be modernised. Existing enterprise awards will cease to operate on 31 December 2013 unless an application to be modernised is made and granted before that date. To date, five applications for modernisation of such awards have been made. Of these, four have been rejected and one (dealing with enterprise awards applying to Telstra Corporation) has been granted. The details of the modern enterprise award for the Telstra Corporation are still in the process of being determined.

The Commission considers that its proposed factors for consideration would provide a sound basis for selecting default superannuation products for listing in all awards, including enterprise awards. However, the treatment of default superannuation products in modern enterprise awards is a matter best left to the discretion of the Default Superannuation Panel, taking into account the views of the relevant parties and FWA more broadly.

## **9.7 Review the new process for selecting default products, including the factors for consideration**

The Commission’s proposed reforms offer the prospect of gains to default fund members and to the community more generally. Nonetheless, as discussed in preceding chapters, changes ensuing from other reform initiatives (particularly the introduction of MySuper) will have implications for default funds and their members. These implications cannot be fully known in advance. And there is inevitably some degree of uncertainty about precisely how the Commission’s proposed reforms will play out in practice, particularly given the uncertainty regarding the number, mix and quality of MySuper products to be offered from 2013.

Against this backdrop, and in keeping with a best-practice policy-making process, the Commission considers that provision should be made for an independent public review of the impact of the proposed new arrangements for selecting default superannuation products for listing in modern awards. A number of participants supported the Commission’s proposed approach to such a review (box 9.5).

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| Box 9.5 Participants’ comments on the proposed review |
| Participants generally supported the Commission’s proposed approach to review.  The CSSA agrees … that there is merit in conducting an independent public review after the first wholesale reassessment of funds, to ensure that the criteria for default fund selection remain useful and relevant and that the selection process is working as intended. (sub. DR56, p. 5)  Ai Group supports this [review] proposal but this should not prevent any problems which become apparent being addressed at an earlier time. (sub. DR79, p. 8)  Others supported the concept of a review, but suggested that it should be conducted much earlier than 2023.  The T.I.S. Fund disagrees with the recommendation that the new system should be reviewed in 2023. Any new system should be reviewed within 5 years of the date it is implemented to prevent the consolidation of a bad system. (Transport Industry Superannuation Fund, sub. DR91, p. 2)  Others questioned whether it was possible to meaningfully consider the timing and content of a review planned that will not occur for over a decade.  ISN questions the utility of proposing a specific date and broad terms of reference for a review in eleven years time. It is likely that there will be considerable change within the industry and its regulatory environment in the intervening period. ISN has no fundamental objection to recommendation 9.3, however, we propose a less prescriptive approach which simply recognises that there should be a future review of the arrangements for the selection of default funds. This could be a stand-alone review, or be part of a future wider superannuation review. (ISN, sub. DR62, p. 28)  ACCI suggested that the need to review the factors for consideration may increase over time, because mergers will lead to increasing diversity in the membership of each fund (sub. DR83). |
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### Timetable for the review

In chapter 8, the Commission re­­commends that the list of default superannuation products in awards be the subject of a wholesale reassessment every four to eight years, following an initial selection process which would ideally commence in 2014.

Reviewing the process and factors for consideration before the first periodic reassessment of all awards has been completed would appear to be premature. Instead, the Commission considers that reviewing the process and factors for consideration after they have been applied at least twice for each award would be appropriate. Ideally, the review would be conducted in 2023.

The Commission recognises, however, the importance of flexibility, particularly where there may be a need to respond to any unforseen effects of the new selection system or to significant consolidation in the superannuation system. As such, any legislated review timetable should provide for the ability to schedule the review before 2023, should the need arise. Conversely, should the initial selection process occur later than 2014, there would need to be flexibility to delay the review beyond 2023.

### Who should undertake the review?

Rather than specify who should conduct a review that is recommended to occur in a decade’s time, it is more appropriate to specify the characteristics of the reviewer. The Commission considers the review should be undertaken by a body that:

* is independent of industrial parties and superannuation funds
* has relevant skills and expertise
* has the capacity to provide a transparent public review.

This could be a stand-alone, independent review, or be conducted as part of any future review of the broader superannuation system.

Recommendation 3

An independent public review of the arrangements for the selection and ongoing assessment of default superannuation products for listing in modern awards should be conducted after the first periodic reassessment of products listed in awards has been completed, ideally in 2023. Amongst other things, the review should examine:

* whether the factors considered in selecting products for listing in modern awards remain useful and relevant
* whether the selection process is working to deliver outcomes that are in the best interests of employees who derive their default superannuation product in accordance with a modern award
* the appropriateness of employers being able to use any MySuper product as a default superannuation product.