



Australian Government
Productivity Commission

Superannuation: Assessing Competitiveness and Efficiency

Productivity Commission
Issues Paper

July 2017

The Commission has released this issues paper to assist individuals and organisations to prepare submissions.

It contains and outlines:

- the scope of the inquiry
- the Commission's procedures
- matters about which the Commission is seeking comment and information
- how to make a submission.

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The Commission has released this issues paper to assist individuals and organisations to prepare submissions to the inquiry. It contains and outlines:

- the scope of the inquiry
- the Commission's procedures
- matters about which the Commission is seeking comment and information
- how to make a submission.

Participants should not feel that they are restricted to comment only on matters raised in the issues paper. The Commission wishes to receive information and comment on issues which participants consider relevant to the inquiry's terms of reference.

Key inquiry dates

Receipt of terms of reference	30 June 2017
Due date for submissions	21 August 2017
Release of draft report	January 2018
Draft report public hearings	March 2018
Final report to Government	June 2018

Submissions can be lodged

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The Productivity Commission

The Productivity Commission is the Australian Government's independent research and advisory body on a range of economic, social and environmental issues affecting the welfare of Australians. Its role, expressed most simply, is to help governments make better policies, in the long term interest of the Australian community.

The Commission's independence is underpinned by an Act of Parliament. Its processes and outputs are open to public scrutiny and are driven by concern for the wellbeing of the community as a whole.

Further information on the Productivity Commission can be obtained from the Commission's website (www.pc.gov.au).

Terms of reference

EFFICIENCY AND COMPETITIVENESS OF THE SUPERANNUATION SYSTEM

I, Scott Morrison, Treasurer, pursuant to Parts 2 and 3 of the *Productivity Commission Act 1998*, hereby request that the Productivity Commission undertake an inquiry to assess the efficiency and competitiveness of Australia's superannuation system.

Background

Today, superannuation is a \$2 trillion sector. It is important that, given the sheer size of the superannuation system, combined with its compulsory and broad nature, the system is efficient. Competition is also important as it can drive efficient outcomes for price, quality and innovation. Small changes in the system can have a real impact on people's standard of living in retirement.

Following the Government's response to Financial System Inquiry Recommendation 10 on efficiency in superannuation, on 17 February 2016 the Government tasked the Productivity Commission to develop criteria to assess the efficiency and competitiveness of the superannuation system (Stage 1) and to develop alternative models for allocating default fund members to products (Stage 2).

These Terms of Reference task the Commission to review the performance of the superannuation system against the criteria identified through the Commission's Stage 1 report, published in November 2016. This will be the third and final Stage of the review.

Scope

The Commission is to assess the efficiency and competitiveness of Australia's superannuation system and make recommendations to improve outcomes for members and system stability. The Commission is to also identify, and make recommendations to reduce, barriers to the efficiency and competitiveness of the superannuation system.

The assessment should be based on the five system-level objectives, 22 assessment criteria, and 89 corresponding indicators set out in the Commission's Stage 1 report.

In undertaking its assessment the Commission should evaluate the accumulation, transition and retirement phases of superannuation as well as the default, choice (including self-managed) and corporate fund member segments.

Whilst not out of scope, defined benefit funds should not be a key focus of the Commission's assessment.

Without limiting the Commission's assessment on the basis of the framework outlined in its Stage 1 report, the Commission should consider the following matters:

Costs, fees and net returns

The Commission is to focus on assessing system-wide long-term net returns, including by reference to particular segments. Through this assessment, the Commission should have particular regard to:

- whether disclosure practices are resulting in a consistent and comparable basis for meaningful comparisons to be made between products;
- whether additional disclosure would improve outcomes for members;
- whether the system is minimising costs and fees (including, but not limited to exit fees) for given returns;
- what impact costs and fees have on members with low account balances, and what actions could be undertaken – whether by funds or policy changes – to ensure that these balances are not eroded needlessly; and
- whether tailoring of costs and fees for different member segments would be appropriate.

Default fund members

In relation to default fund members, the Commission should consider:

- whether the current default settings in the system are appropriate, or whether policy changes would be desirable; and
- whether an alternative default fund allocation mechanism should be introduced that would deliver net benefits.

Insurance in superannuation

The Commission should consider the appropriateness of the insurance arrangements inside superannuation, including:

- the impact of insurance premiums on retirement incomes of both default cover and individually underwritten cover funded inside of superannuation;
- the extent to which current policy settings offset costs to government in the form of reduced social security payments;
- whether policy changes could improve default cover through superannuation, so that default cover:
 - provides value-for-money;
 - does not inappropriately erode the retirement savings of members of all ages; and
 - delivers consistent outcomes across the system; and
- whether policy changes are needed to ensure that insurance is not a barrier to account consolidation.

The broader financial system

In response to the 2014 Financial System Inquiry, the Government agreed to periodic reviews of competition in the financial sector. Pursuant to this response, the Government has also tasked the Commission to conduct an inquiry into competition in the financial system more broadly.

The two inquiries should not duplicate analysis or reporting.

Process

This review will commence on 1 July 2017.

Surveys involving industry participants should be tested with stakeholders before being implemented, to limit collection costs and ensure respondents consistently interpret data requirements.

The Commission should consult widely and undertake appropriate public consultation processes, including inviting public submissions and holding public hearings.

The Commission should release a draft report in January 2018 and provide its final report to the Government within 12 months of the commencement of the review.

Scott Morrison
Treasurer

[Received 30 June 2017]

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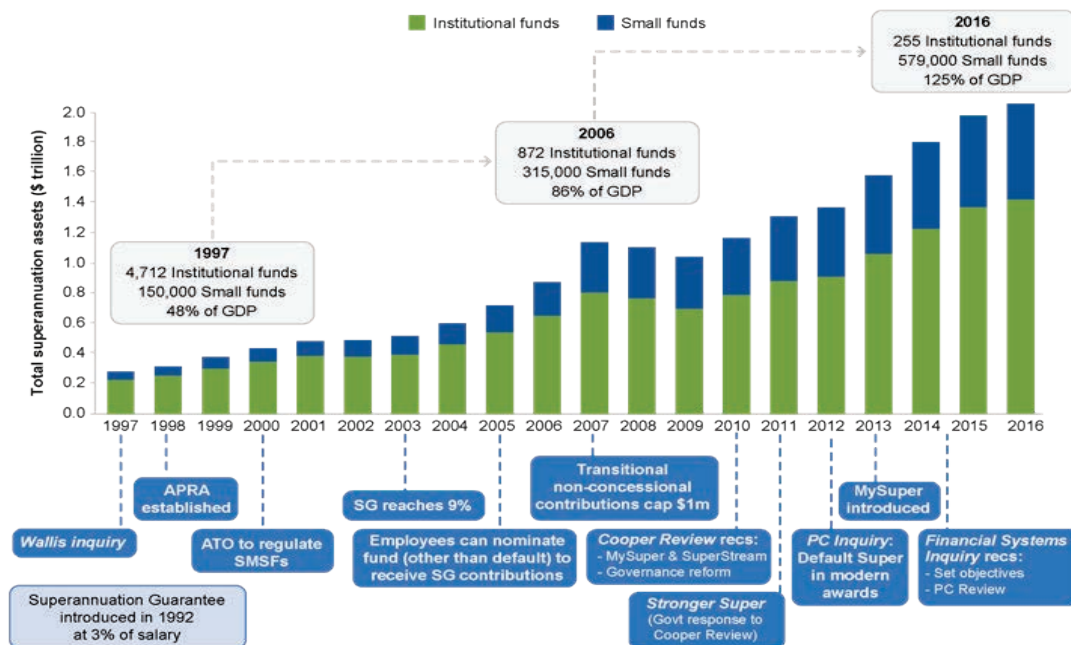
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1 What is this Inquiry about?

This Inquiry will assess the competitiveness and efficiency of the Australian superannuation system. The Australian superannuation system has grown rapidly since the introduction of the Superannuation Guarantee in 1992, both in terms of funds under management and coverage (figure 1). Almost all employed Australians contribute to (their) superannuation. Collectively, Australians have over \$2 trillion of assets in superannuation funds, comprising about 20 per cent of total household assets. In relation to the financial system as a whole, superannuation will continue to increase in relative importance as the system matures by the 2040s.

The sheer size of the superannuation system, combined with its compulsory and broad nature, makes the efficiency of the system paramount. Even small changes in the efficiency of the system can have significant impacts on the wealth and wellbeing of Australians. Competition is often the impetus to promote efficiency and members' best interests — an important means to a wellbeing end.

Figure 1 Key developments in the superannuation system^a

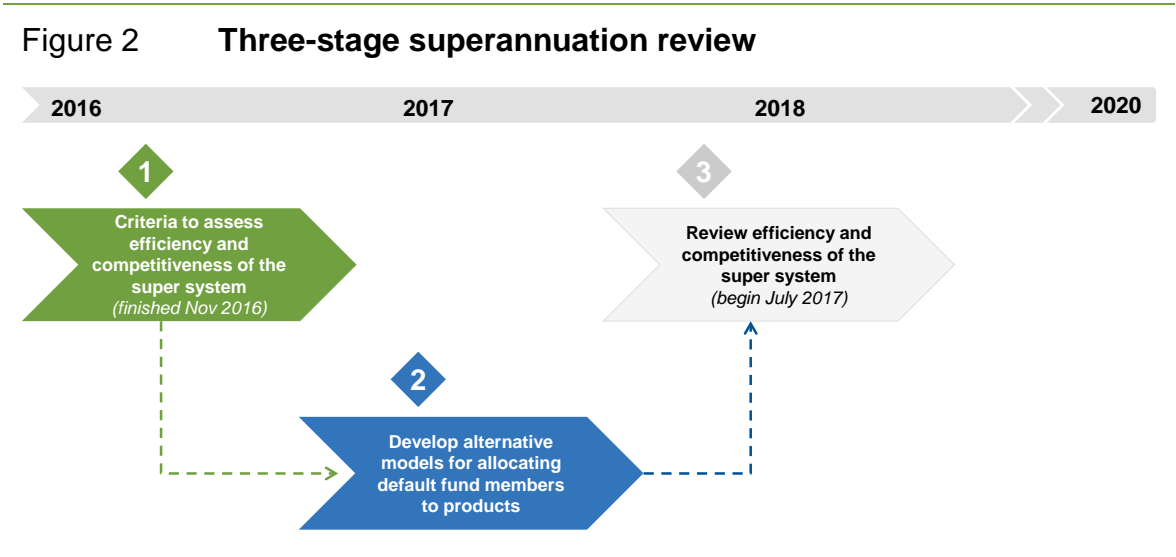


^a 'Institutional funds' comprise corporate, industry, public sector and retail funds. 'Small funds' comprise small APRA funds, single-member approved deposit funds and self-managed superannuation funds.

Data sources: ABS (*Australian National Accounts: National Income, Expenditure and Product, Australia, June 2016*, Cat. no. 5206.0); APRA (2007, 2014, 2016a, 2016b).

What has the Commission been asked to do?

In early 2016, the Government tasked the Commission to begin a three-stage process to assess the competitiveness and efficiency of the superannuation system (figure 2). This review stems from a recommendation made by the 2014 Financial System Inquiry.



The **stage 1** Study involved developing criteria to assess whether, and the extent to which, the superannuation system is efficient and competitive in delivering the best outcomes for members. In November 2016, the Commission published its final report, detailing these criteria — *How to Assess the Competitiveness and Efficiency of the Superannuation System* (PC 2016). The publication of these criteria provided transparency and certainty to the superannuation industry about how it will be assessed ahead of the future review — stage 3.

The **stage 2** Inquiry involved developing alternative models for a formal competitive process to allocate default superannuation members to products. The intention of the second stage was for these models to provide workable alternatives for the Government’s consideration, and be an input to stage 3.

Subsequently, and in the context of issuing the Terms of Reference for stage 3, the Treasurer has agreed with the Commission’s request that the stage 2 work be incorporated into and finalised as part of stage 3’s broader review of the competitiveness and efficiency of the system. No final Inquiry report from stage 2 will be issued separately, and instead final advice on its subject matter will be provided in the final report for the stage 3 Inquiry, now commencing.

The Commission's draft report *Superannuation: Alternative Default Models* detailed four potential alternative default allocation models. Consultation followed by way of second round submissions and public hearings.¹

Amongst other participant feedback on the draft, a near consensus view was for the Commission to ultimately assess the alternative models alongside the current arrangements. And the Terms of Reference for the stage 3 Inquiry do allow for that.

Participant feedback on the draft report, by way of submissions and public hearings, has been used to refine the alternative models presented in the *stage 2* draft report. The four options have not changed materially from those presented in the draft report and they will now be incorporated for broader consideration as part of the current Inquiry.

As one of the tasks for stage 3, the Commission will:

- assess the current default arrangements against the same baseline of no defaults, and consistently apply the same model assessment criteria
- examine the relative merits of the current default arrangements vis-à-vis the alternative model(s)
- subject to the above, make recommendations on what (if any) changes should be made to the current default arrangements, or whether an alternative default model should be introduced.

This **stage 3** Inquiry is the final stage of the Commission's superannuation work initiated by the Financial System Inquiry. The purpose of this Inquiry is to use the criteria developed in the first stage to review the competitiveness and efficiency of the superannuation system. This Inquiry follows the full implementation of the MySuper reforms which required that all default products meet certain requirements by 1 July 2017.

2 How will the super system be assessed?

There is little precedent here (and internationally) for reviewing the competitiveness and efficiency of a superannuation or pension system in its totality. The broader efficiency and system-wide perspectives are both unique and make this a challenging task.

In its stage 1 Study, the Commission consulted extensively with participants on the development of an assessment framework to be applied, including through meetings, submissions and roundtables. The resultant framework was broadly supported by participants and international observers.

¹ In its draft report, the Commission also flagged that it was undertaking an experimental survey of members to add to its evidence base to inform the assessment and refinement of the alternative models. The results from that survey have now been published on the Commission's website.

The Australian Productivity Commission is to be commended for its work in thinking through the proper goals of a pension system and how goal achievement should be benchmarked ... its work is not only relevant in Australia, but in other countries with developed pension systems as well ... (Ambachtsheer 2017, p. 4)

This section provides a brief recap of the key elements of the assessment framework that will be applied by the Commission in the current (stage 3) Inquiry. For further details on how this framework was developed, participants should refer to the stage 1 report: <http://www.pc.gov.au/inquiries/current/superannuation/competitiveness-efficiency#report>.

What is the system?

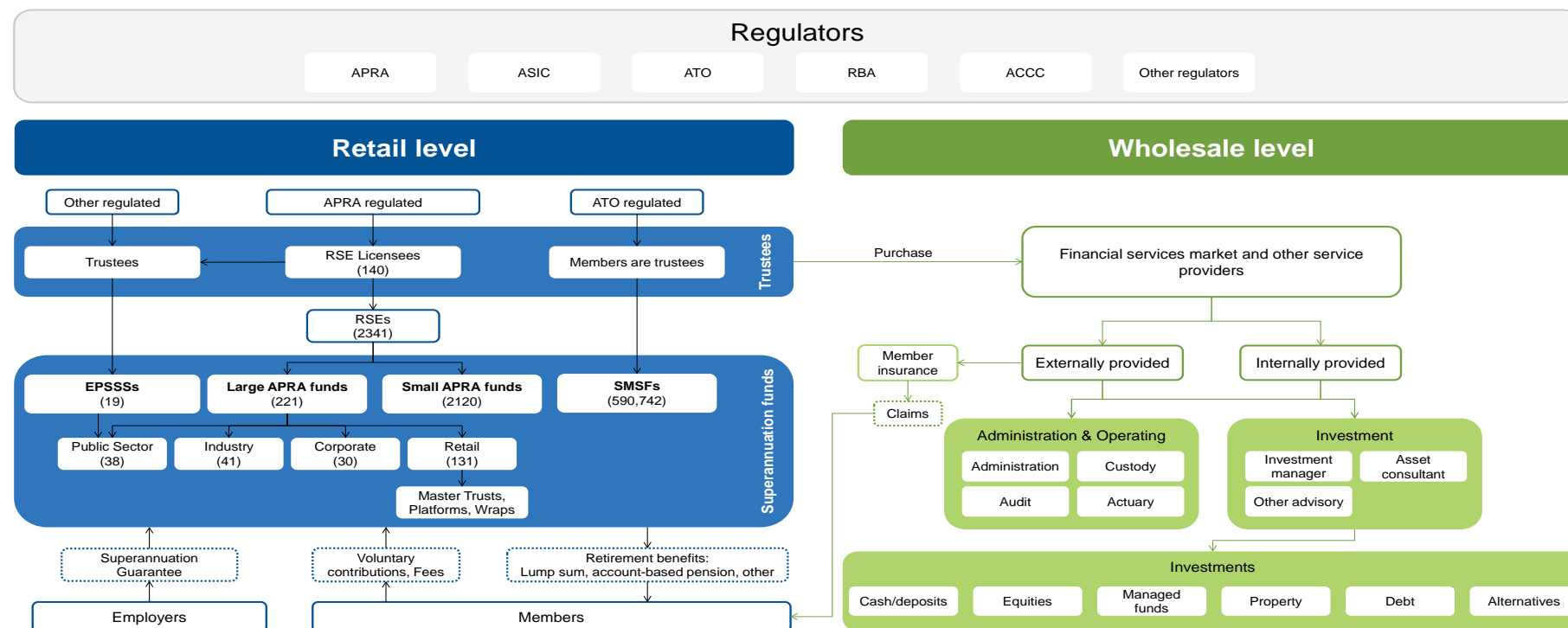
The superannuation system is bigger than just the superannuation funds (the industry). It encompasses many horizontal and vertical relationships on the supply side at the wholesale and retail levels, the decisions of members and their intermediaries on the demand side (over the phases of superannuation), and the actions of regulators on both the supply and demand sides (figure 3).

Three matters are important to reiterate. First, the Commission's focus will not be on comparing and ranking the performance of individual products or funds. The task is a system-wide assessment. The Commission's analysis will, at times, examine the performance of specific segments of the superannuation system — such as the default, self-managed superannuation fund (SMSF) and retirement segments — but only where this will meaningfully inform the system-wide analysis.

Second, this review will examine all components of the superannuation system, not just the superannuation fund (trustee) level. This includes not only service providers at the upstream (wholesale level), but importantly the activities and influences of members, employers and regulators. However, examination of these other parts of the system will be undertaken where this is materially relevant — that is, specific issues will be examined if there is evidence of potential problems which have a bearing on the competitiveness and efficiency of the system. Thus, broad participation in this Inquiry by a variety of participants is very important.

Third, and most importantly, notwithstanding the broad and complex nature of the superannuation system and the many participants within it, the Commission's overriding focus will be on the outcomes for members. This will be the guiding principle for the assessment and any policy recommendations that arise out of this Inquiry.

Figure 3 The superannuation system^{a,b,c}



^a Numbers in brackets denote number of trustees or superannuation funds as reported by APRA as at March 2017. ^b RSEs are Registrable Superannuation Entities; EPSSSs are exempt public sector superannuation schemes; and SMSFs are self-managed superannuation funds. ^c Small APRA funds includes pooled superannuation trusts and single member approved deposit funds for the purposes of this figure

Data source: APRA (2017).

How will this Inquiry interact with the Inquiry on Competition in the Australian Financial System?

Separate to this Inquiry, the Commission has been asked to undertake an Inquiry into Competition in the Australian Financial System. This distinct 12-month Inquiry also commenced on 1 July 2017 and will run concurrently with the Commission's review of the superannuation system.

The Commission recognises the various linkages between the superannuation system and the financial system — as superannuation matures further it will continue to increase in relative importance in the broader financial system. In developing the assessment framework in stage 1, the Commission was cognisant to consider if (and how) these linkages could impact the competitiveness and efficiency of the superannuation system. This is reflected in aspects of the Commission's assessment framework. For example, the efficiency assessment will include consideration of whether there are systemic risks in the superannuation system (which could have implications for broader financial system stability), while the competition assessment will consider the impact of vertical and horizontal integration in the superannuation system, and the nature and extent of competition in upstream service provider markets used by superannuation funds.

The Commission's review of the superannuation system will be undertaken separately and in parallel to the inquiry into competition in Australia's financial system. The respective Inquiry teams within the Commission will collaborate to avoid duplication of analysis or reporting.

The Commission's assessment approach

The Commission's approach to assessing the superannuation system developed in the stage 1 Study involves three steps:

1. defining *system-level objectives* — what is the superannuation system trying to achieve?
2. formulating *assessment criteria* based on these objectives — that is, the performance standards by which to assess if the system-level objectives have been achieved
3. identifying corresponding *indicators* to facilitate the assessment.

Defining the system-level objectives

What is efficient ultimately depends on what you are trying to achieve, that is the objectives of the superannuation system. The Australian Government has announced that the objective of superannuation is 'to provide income in retirement to substitute or supplement the Age Pension' and has introduced a bill into the Parliament to enshrine this in legislation (Australian Government 2016).

With this overarching objective in mind, the Commission developed five system-level objectives that are within the scope of influence of the superannuation system and specific to the principles of competitiveness and efficiency (table 1). Four of the objectives link to the different dimensions of economic efficiency — operational, allocative and dynamic efficiency. Another objective is that competition should drive efficient outcomes (PC 2016). This last objective makes clear that competition is not an end in itself, but an intermediate objective insofar as it drives more efficient outcomes for members.

Formulating the assessment criteria

Linked to each objective is a set of assessment criteria, 22 in total (table 1). These criteria are formulated as questions that aim to identify attributes that a competitive and efficient superannuation system would be expected to possess. Assessment against the criteria will provide insights into whether each system-level objective is being met.

In developing these criteria, the Commission treated the broad policy settings that govern the system and other limbs of retirement incomes policy as given. This is done either by omission (the Commission is not proposing to assess the system on what is outside its influence, such as the overall adequacy of retirement incomes) or by recognising the influence of external factors when proposing criteria. This does not preclude the Commission from assessing the effect of policy on the competitiveness and efficiency of the system in this stage 3 Inquiry.

Developing indicators to assess each criterion

The Commission identified a comprehensive suite of 89 unique indicators. They can be thought of as the evidence base the Commission will draw on in evaluating each criterion. The indicators vary in type and nature. Some are focused on inputs into and observed behaviours in the system, while others identify outputs and outcomes from the system. Some indicators can be measured quantitatively while others will require a qualitative assessment.

The evaluation of certain indicators will draw heavily on benchmarking. Performance will be benchmarked against others, against stipulated objectives, or over time. In some parts of the assessment, the Commission will complement its benchmarking with a ‘negative test’ — an examination of the barriers that may be impeding the competitiveness and efficiency of the system (such as barriers to entry).

Table 1 System-level objectives and assessment criteria

<i>Assessment criteria</i>	<i>Number of indicators^a</i>
System-level objective #1: The superannuation system contributes to retirement incomes by maximising long-term net returns on member contributions and balances over the member's lifetime, taking risk into account	
E1. Are long-term net investment returns being maximised over members' lifetimes, taking account of risk?	4
E2. Are costs incurred by funds and fees charged to members being minimised, taking account of service features provided to members?	10
E3. Do all types of funds have opportunities to invest efficiently in upstream capital markets?	4
E4. Is the system effectively managing tax for members, including in transition?	3
E5. Are other leakages from members' accounts being minimised?	5
System-level objective #2: The superannuation system meets member needs, in relation to information, products and risk management, over the member's lifetime	
E6. Is the system providing high-quality information and intrafund financial advice to help members make decisions?	7
E7. Is the system providing products to help members manage risks over their life cycles and optimally consume their retirement incomes?	7
E8. Are principal-agent problems being minimised?	7
System-level objective #3: The efficiency of the superannuation system improves over time	
E9. Does the system overcome impediments to improving long-term outcomes for members?	6
E10. Are there material systemic risks in the superannuation system?	3
System-level objective #4: The superannuation system provides value for money insurance cover without unduly eroding member balances	
E11. Do funds offer value for money insurance products to members?	10
E12. Are the costs of insurance being minimised for the level and quality of cover?	7
System-level objective #5: Competition in the superannuation system should drive efficient outcomes for members	
<i>Market structure</i>	
C1. Is there informed member engagement?	8
C2. Are active members and member intermediaries able to exert material competitive pressure?	7
C3. Is the market structure conducive to rivalry?	2
C4. Is the market contestable at the retail level?	3
C5. Are there material anticompetitive effects of vertical and horizontal integration?	6
<i>Conduct and outcomes</i>	
C6. Do funds compete on costs/price?	6
C7. Are economies of scale realised and the benefits passed through to members?	5
C8. Do funds compete on member-relevant non-price dimensions?	5
C9. Is there innovation and quality improvement in the system?	3
C10. Are outcomes improving at the system level?	2

^a Many indicators are used multiple times. In total there are 89 unique indicators.

The Commission's stage 1 report is careful to acknowledge that some indicators are ambiguous and cannot (and will not) be interpreted in isolation. Robust evidence and judgment will be required to interpret the meaning of each indicator. In some cases, this meaning may only surface in the presence of other indicators. The indicators will be

considered and interpreted collectively to inform the assessment. The Commission's set of system-level objectives and criteria are summarised in table 1 below, while the full set of objectives, criteria and indicators can be found in attachment B.

3 How can you contribute to this Inquiry?

The Commission appreciates the contributions made by participants of the stage 1 Study in the development of its assessment framework. The Commission is keen to also secure the participation of superannuation members for this Inquiry.

Notably, the Commission's consultation with participants in stage 1 is effectively the initial consultation for this stage 3 Inquiry. With the benefit of that early groundwork and consultation, this issues paper poses two types of questions for participant comment — *general questions* for all interested participants and *technical questions* for those with the technical expertise on the more methodologically complex parts of the assessment.

As discussed earlier, the Commission considers its assessment framework to be comprehensive and robust. The framework itself covers the 'lion's share' of the Commission's assessment task as articulated in the Inquiry's Terms of Reference. The Commission has identified some areas that may require evidence supplementary to the framework and they are outlined below.

There are two primary ways participants can contribute to this Inquiry given the context of the framework developed in stage 1. Participants can contribute to the:

- identified evidence base to underpin the assessment
- methodology for deriving or interpreting particular indicators.

The Commission is also seeking participant feedback on the performance of the current system for allocating default members to products using the assessment approach developed in stage 2 (discussed later in this section).

As is standard with the Commission's Inquiry processes, participants can contribute through a number of avenues including submissions, brief comments on the inquiry website, roundtables and/or public hearings.

Initial submissions are due by 21 August.

Contributions to the evidence base

In its stage 1 Study, the Commission set out the evidence base required for this review. The Study noted that the vast majority of the evidence is in the public domain (for example, regulator data or fund disclosures) or is available for purchase (for example, data collected by research firms). The Commission has identified that nearly half of stage 3 data needs

are already in the public domain, that more than one third are available for purchase by the Commission, with less than 20 per cent needing to be collected from funds or members.

The stage 1 report also identified several constraints pertaining to the availability, quality and comparability of data, which the Commission would need to take into account. The Commission would greatly appreciate the assistance of participants in filling some of the data gaps that cannot be filled by other means. Nonetheless, the Commission reiterates that it will initiate and do most of the heavy lifting on the evidence collection and collation.

What additional sources of evidence will the Commission draw on?

The Commission's evidence sources (additional to those that were in the public domain at the time of stage 1) and indicative timelines for their collection are detailed in figure 4.

Case studies can provide valuable evidence of the experiences of participants — both from a member and the industry perspective. Several of the Commission's indicators rely on case studies to provide insights into how the superannuation system is functioning, especially where indicators are qualitative in nature.

As identified in the stage 1 report and the Terms of Reference for this Inquiry, the Commission also intends to draw on specially designed surveys for some of its evidence base. It intends to conduct three surveys — a survey of members, a survey of superannuation funds and a survey of fund CEOs (box 1). The surveys will focus on relevant evidence gaps and will be designed to minimise the compliance burden on participants. The results will be de-identified to protect the confidentiality of respondents.

The Commission will ensure that draft surveys are pilot tested before they are rolled out, and will draw on the survey results in its draft report. The Commission anticipates universal participation in the fund and fund CEO surveys. Ultimately, the information gathered will be of assistance to all, especially in addressing existing evidence gaps. The Commission will publish the twin list of fund and fund CEO survey recipients and survey respondents. The Commission also notes its information gathering powers for inquiries of this nature under the *Productivity Commission Act 1998* (Cwlth).

The Commission also expects to rely on unpublished data, evidence and analysis of all of the key agencies responsible for regulating and/or monitoring the superannuation system, including APRA, ASIC, ATO, ACCC and the RBA. The Commission welcomes submissions from all of those agencies.

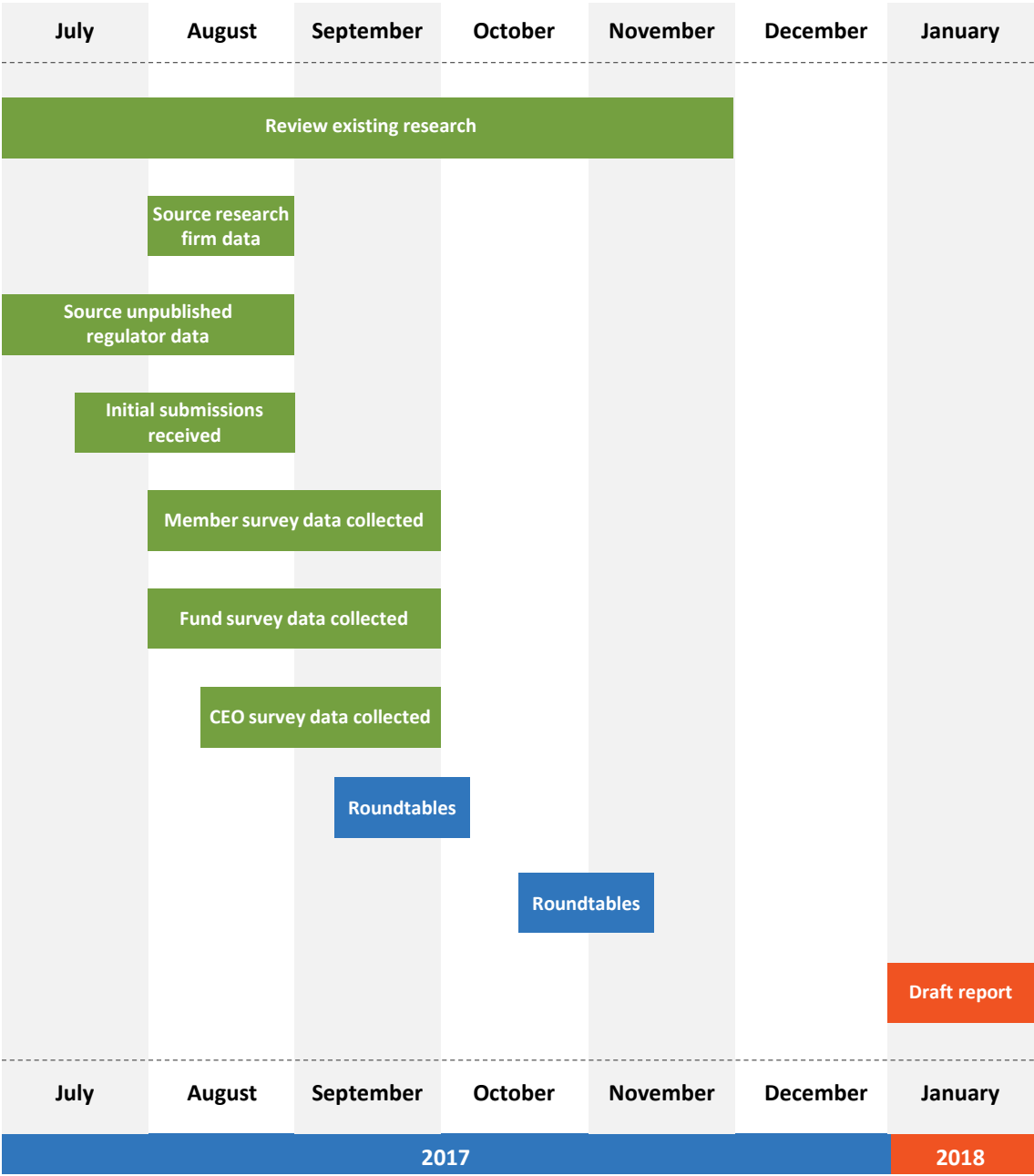
Subsequent sections of this issues paper identify some evidence gaps that could be best addressed by specific agencies. The Commission will consult directly with those agencies on how they could best contribute to this Inquiry.

Finally, the Commission intends to conduct several technical roundtables to test and refine its approach to measurement and interpretation of particular indicators (discussed further below in the section on methodology and interpretation).

In using those evidence sources, the Commission will be mindful of preserving confidentiality of any commercially sensitive material.

In the context of responding to this issues paper, the Commission is also keen for participants to provide their experiences through case studies, and suggest any existing research or reviews that are particularly important evidence sources.

Figure 4 Additional evidence sources and indicative collection timelines



The Commission wants to hear from members

Throughout this Inquiry, the Commission wants to hear from members (including owners of SMSFs) about their experiences with the system. Participants can make a formal submission or simply leave a brief comment on the Inquiry web page — there is no prescribed length or format for such contributions, as long as they are relevant to the Inquiry. To assist this process, the Commission has prepared a list of topics and questions in the next section on which contributions and member feedback would be particularly valuable.

Box 1 **Surveys to be conducted for this Inquiry**

In its stage 1 Study, the Commission identified a number of relevant recent surveys of system participants that it expects to use in the stage 3 Inquiry. In particular, it noted several surveys that tested the experiences of SMSF owners (PC 2016, appendix G). The Commission also anticipated the need to conduct its own surveys of funds and members, with the final decision to be made at the time of this review. After considering the available evidence, the Commission will proceed with three surveys targeted at different participants within the superannuation system: a survey of members (including SMSF owners), a survey of superannuation funds (ultimately the fund trustees) and a survey of fund CEOs in their individual capacity. The member survey and the fund survey will have areas of overlap to assess member system relative to trustee perceptions.

Survey of members

The member survey will collect data on about 20 indicators (identified in attachment B), which cover various aspects of member experience with the superannuation system. Specifically, it will focus on the following assessment criteria:

- informed member engagement (C1)
- the degree to which active members are exerting competitive pressure (C2)
- whether funds are competing on member-relevant non price dimensions (C8)
- improving outcomes at the system level (C10)
- availability of information and intrafund advice to enable sound decisions (E6)
- resolution of principal–agent problems (E8)
- provision of value for money insurance (E11).

(continued next page)

Box 1 (continued)

Survey of funds

The survey will be directed at trustees of all large APRA-regulated funds (funds with more than 4 members) and will collect data on about 20 indicators, identified in attachment B. It will have areas of overlap with the member survey on member-related indicators under criteria C1, C8, E6, E8 and E11. In addition, it will focus on several fund-specific indicators, under the following criteria:

- market contestability and barriers to entry (C4)
- materiality of anticompetitive effects from vertical and horizontal integration (C5)
- innovation and quality improvement in the system (C9)
- provision of products to manage life-cycle risks (E7)
- overcoming impediments to improving long-term member outcomes (E9)
- minimisation of insurance costs for the level and quality of cover (E12).

Survey of fund CEOs

The Commission will also undertake a survey of all CEOs of large APRA-regulated funds focusing on fund governance. The Commission's approach will be informed by relevant international methodology used in comparable governance surveys.

Key evidence needs and priority areas for submissions

A threshold evidence issue for the Commission relates to the effect of policy settings on system performance. As noted above, the stage 1 report deemed the existing policy settings governing the system as given, but flagged that stage 3 would assess the extent to which those policy settings inhibit the competitiveness and efficiency of the system. The Commission now invites participant comment on this issue.

POLICY IMPEDIMENTS: GENERAL QUESTION FOR PARTICIPANTS

What are the material policy or regulatory impediments to the competitiveness and efficiency of the superannuation system? Please relate your comments to the relevant assessment criteria (in the Commission's assessment framework) and provide evidence of how and to what extent those policy impediments affect performance as measured by the related indicators.

In developing the assessment framework, the Commission reviewed publicly available evidence and selected a list of areas where it expected a need for additional evidence. This analysis has been updated to reflect ongoing research by others and regulatory

developments.² It also captures the few additional areas needed to fully address the Inquiry's terms of reference. For convenience, additional evidence needs are presented in two tables.

- Table 2 reflects the priority areas for **submission** evidence and who the Commission would expect to address them. The Commission has also provided a list of guidance questions for members below.
- Table 3 (attachment A) reflects all other additional evidence and how it will be collated.

The full list of indicators and corresponding evidence sources developed in stage 1 is in attachment B.

SUBMISSION EVIDENCE: GENERAL QUESTION FOR INDUSTRY PARTICIPANTS AND REGULATORS

Please provide case study and other evidence to address the evidence needs identified in table 2 as being relevant to you.

² For example, the Commission is monitoring the implementation and effect of the RG97 disclosure standards and the ongoing work and consultation of the Insurance in Superannuation Working Group to develop a Code of Practice for insurance. The Commission will also draw on the work recently undertaken by ASIC (2017) on member experience in superannuation.

Table 2 Priority areas for submission ‘case study’ and other evidence

<i>Evidence required</i>	<i>Expected evidence sources</i>
Member behaviour and knowledge	
Member account activity and account monitoring	Case study evidence from funds and members
Insurance	
Ease and extent of members opting out of insurance, amending cover or making claims	Case study evidence from funds and members; evidence from Insurance in Superannuation Working Group
Funds' use of member information to provide default insurance cover	Case study evidence from funds and members; evidence from Insurance in Superannuation Working Group
Contestability	
Height of barriers to entry arising from default rules and market impediments to funds accessing distribution channels	Case study evidence from funds
Fund behaviour	
Funds' use of member information and behavioural finance lessons in product design, development and take-up of tailored products, member services and retirement income products	Case study evidence from funds
Effect of regulation	
For ASIC: <ul style="list-style-type: none"> • overall member experience • regulator monitoring and enforcement activity on inducements • ongoing and predicted effect of RG97 on transparency of fee disclosure 	Relevant unpublished evidence from regulator; case study evidence from funds and members
For APRA: <ul style="list-style-type: none"> • effect of current successor fund transfer rules and likely effect of proposed guidelines on fund mergers • regulator activity in ensuring that trustees discharge their obligations under the scale test • regulator activity in ensuring that trustees discharge their obligations on bundled insurance 	Relevant unpublished evidence from regulator; case study evidence from funds and members

Overall impressions

Are you satisfied with how the system has performed for you and do you trust it to deliver you the best outcomes in retirement?

How you engage with your superannuation

How closely do you follow the performance of your superannuation account? What is the main way you interact with your fund? What member services do you find most useful and why?

What other information sources do you use to make decisions about your super?

How easy is it to research and switch to a new product and/or provider? What are the main hurdles that could be removed to make the task easier?

If you are a retiree, how well is the system addressing your needs to manage the super savings you have accumulated and assist you in making decisions about a retirement income product?

For SMSF members, what was your main motivation for establishing an SMSF? Do you still retain an account with an institutional fund as well, and if so, why?

How funds engage with you

Do you trust your current fund(s) to keep you informed about the performance of your product and other options within the fund?

How accessible, comparable and easy to understand is the information on fees and features for your product and across the system more broadly? Has this changed over the time you have been with a fund?

How comfortable are you that the current level and nature of advertising and other marketing activity by superannuation funds is promoting your interests as a member? Have you encountered any marketing activity that is problematic?

Insurance in superannuation

How comfortable are you to allocate a portion of your superannuation savings to life and total and permanent disability insurance? How would you determine how much to allocate to insurance?

If you have used your superannuation insurance policy, how would you rate your experience?

How easy is it to amend or opt out of the insurance policy offered as a default by your fund?

Have you retained duplicate superannuation accounts for the purpose of retaining an insurance policy attached to a previous superannuation product?

Contribute to methodology and interpretation

Collectively, the assessment framework's criteria and indicators developed in stage 1 are intended to inform a detailed and working understanding of the competitiveness and efficiency of the superannuation system. But applying the indicators to draw conclusions about the system overall will be challenging.

The Commission has identified two areas in particular where feedback from participants on the methodology to be applied would add the most value at this stage.

Estimating the utilisation and pass through of economies of scale

As discussed in the stage 1 report, the utilisation of economies of scale and the pass through of the benefits to members is an important criterion for effective competition and a key determinant of member outcomes. The stage 1 report flagged that econometric approaches will be used to estimate two indicators related to scale economies:

- unused scale economies at the fund level
- pass through of benefits from scale economies (wholesale and retail) to members.³

The first indicator involves estimating the relationship between fund-level costs and size (in terms of funds under management and number of members). Broadly speaking, this involves several steps:

- specification of a cost function for regression, controlling for a range of factors and accounting for the possibility of selection (survivorship) bias in the data
- evaluation of whether estimated costs (from the above step) would be lower if there was greater consolidation of funds.

The second indicator is then estimated by:

- using the estimated cost functions (from above) to estimate 'realised scale economies' — that is, the benefits (lower costs) attributable to changes in scale
- evaluating whether they have been passed through to members in the form of lower fees (controlling for fund-level fixed effects and other factors that affect fees, where possible).

³ The stage 1 report also discussed several approaches used in the literature to estimate scale economies.

SCALE ECONOMIES: TECHNICAL QUESTIONS FOR PARTICIPANTS

What methodology would you use to estimate unused scale economies and pass through of realised scale economies, and why? What challenges would need to be overcome with that approach? How material are issues around selection (survivorship) bias and how could this be controlled for? How should the level of merger activity in recent years be factored into the analysis and the interpretation of results?

Investment performance benchmarking

A key element of the Commission's assessment framework will focus on the historical investment performance of the system. Assessing investment performance (or net returns) requires a point of comparison. As outlined in the stage 1 study (PC 2016, pp. 117–123), the Commission will benchmark long-term net investment returns at the system, segment and asset-class levels (along with a range of other indicators) to inform its overall view of whether long-term net returns are being maximised in the system.

At the *system level (and where relevant, at the segment level)*, the Commission will compare long-term net returns to net returns from a set of passive, liquid reference portfolios (PC 2016, p. 120). This will include a reference portfolio based on average asset allocations across the system for the relevant period. Comparisons will also be made between reference portfolios representative of typical multi-asset products in the system (or segment) associated with different levels of asset allocation, and their respective passive benchmarks. The analysis will take into account equivalent taxes and various fee levels (for robustness testing) associated with a reference portfolio, and will be supplemented by comparison of system-wide net returns to other benchmarks, such as CPI + X targets.

At the *asset-class level*, the Commission will compare long-term returns to specific asset classes to a listed benchmark for each asset class (a sample was set out in table 6.1 of the stage 1 report) (PC 2016, p. 121). The Commission acknowledged in its stage 1 report that there are practical difficulties estimating long-term net returns to specific asset classes across the system. To a large extent, the nature of the analysis will be guided by data availability (attachment A, table 4). The Commission's preferred approach will be to draw on (and aggregate) fund and product-level data in order to generate estimates of long-term net returns to individual asset classes within the system.

BENCHMARKING: TECHNICAL QUESTIONS FOR PARTICIPANTS

On the system-level benchmarking:

- In the context of the approach set out in the stage 1 Study to compare long-term net investment returns to a set of passive, liquid reference portfolios, which reference portfolios would most meaningfully inform the analysis? What is the best way to ensure that equivalent taxes are netted out of returns to a reference portfolio? What fee levels should be applied to the reference portfolio? What are the most appropriate listed asset class benchmarks to use to calculate the returns to these reference portfolios?*

On asset-class level benchmarking:

- In the context of the approach set out in the stage 1 Study to benchmark long-term net investment returns at the asset class level, and given the available data, what is the best way to estimate long-term net returns at the asset-class level for the system, and why? Which listed benchmarks should be used for each asset class? How can the Commission best assess the investment performance of unlisted investments?*
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Technical roundtable

To assist its analysis of the two technical issues discussed above (and any other technical issues the Commission considers necessary as the Inquiry progresses), the Commission will convene a technical roundtable with participants with expertise on these matters to discuss the methodology being applied and data availability.

Questions that are specific to default allocation

Assessing the current arrangements

The Commission will assess the current arrangements for allocating default members to products against the framework that was applied in developing its alternative models in stage 2. The questions below draw on the approach developed in stage 2.

The Commission recognises that existing arrangements, as legislated, differ from existing arrangements as they currently operate. Thus it will assess the current arrangements both ‘in practice’ (today’s implemented arrangements) and ‘in prospect’ (with the legislation fully implemented). For every question below that refers to existing arrangements, participants are requested to comment on **both** in practice and in prospect arrangements.

CURRENT DEFAULT ARRANGEMENTS: GENERAL QUESTIONS FOR PARTICIPANTS

How do the existing default arrangements mitigate the paramount risk of any default system — a member defaulting to a (long-term) underperforming default product? What is the evidence of long-term underperforming default product providers exiting the default market?

How do the existing default arrangements create incentives for funds to maximise long-term net returns and allocate members to products that meet their needs? How could the existing arrangements be improved to achieve this goal?

What is the evidence that existing default arrangements encourage open participation (contestability) and rivalry between funds for the default market (competition for the market)? What is the evidence that there is competitive pressure that drives innovation, cost reductions and more efficient long-term outcomes for members? How could the existing arrangements be improved to achieve this goal?

How do the existing default arrangements promote accountability and integrity in the selection and delivery of default superannuation products? How could the existing arrangements be improved to achieve this goal?

Do the existing default arrangements create any concerns about stability in the superannuation system that could lead to significant systemic risks?

Do the existing default arrangements minimise overall system-wide costs, taking into account costs on members, employers, funds and governments? How could the existing arrangements be improved to achieve this goal?

Transition issues in moving to a new default allocation model

In considering whether an alternative default allocation model is needed and will generate a net benefit for the community, the Commission will consider transition issues and any transition costs. These would likely differ across alternative models and would also depend on the scope of the application of the model (for example, whether it would cover new entrants into the system only or existing members of the system).

Following consultations on the stage 2 draft report, and in particular following claims made in public hearings, the Commission requested advice from APRA on anticipated impacts on the sustainability of funds from adopting any of its alternative default allocation models, as well as from moving to a first-timer defaulting approach.⁴ APRA's post-draft submission (sub. DR101) presented analysis for a five-year period, which indicated that:

... the estimated immediate impact of the loss of the first timer pool and turnover pool of default contributions on its own would be limited. More pronounced impacts are estimated to

⁴ In its stage 2 report, the Commission recommended that members are defaulted into a product once, on joining the workforce and remain in that product unless they actively choose to switch — a first-timer defaulting approach.

occur ... in the third year ... This suggests that RSE licensees would have some opportunity to develop and implement strategies to mitigate potential impacts and ensure appropriate outcomes for members of the RSE.

The Commission further proposed in its stage 2 draft report that if a new model is adopted it would apply only to new entrants to the default market. The Commission requests feedback on transition issues on this basis.

ALTERNATIVE DEFAULT ARRANGEMENTS AND TRANSITION ISSUES: GENERAL QUESTIONS FOR PARTICIPANTS

Which of the four models identified in the stage 2 Inquiry is likely to generate the greatest transition issues and costs, and why?

For the alternative models presented by the Commission, what would be the key transition issues and risks for:

- *members*
- *funds*
- *employers*
- *Government?*

What is your estimate of the costs from those transition issues and how did you arrive at this estimate?

What is the optimal timing and pace of implementation of the alternative model(s) to mitigate transition issues?

Common supporting model features from the stage 2 Inquiry

The Commission's alternative default models set out in the stage 2 draft report were accompanied by a set of proposed features common to all (or at least multiple) models. The Commission has reviewed subsequent participant feedback on these features.

The Commission's approach to settling several model features will benefit from early and targeted consultation as part of this Inquiry to enable their settled form to be incorporated in the stage 3 draft report. The Commission expects to make early calls on the following matters:

- its proposed focus on a simple, low-cost accumulation product for default members
- the proposal for one model (assisted employee choice) to use a 'last resort fund' for employees who fail to make a decision. Participant consultation indicated that this may not be the best way of ensuring good outcomes for employees who failed to exercise choice under the model. The consultation will extend to the suggestion that members who fail to make a decision would be allocated to the default products on the shortlist on a sequential basis, broadly consistent with the approach applied in model 3 (multi-criteria tender) and model 4 (fee-based auction)

-
- the constitution of a new non-ongoing selection body, where the principles were broadly supported by participants, but there was concern that the body might become politicised.

ALTERNATIVE DEFAULT ALLOCATION MODELS: GENERAL QUESTION FOR PARTICIPANTS

How could the process for constituting the body for selecting default products be designed to deliver accountability (and thus not be judicial in nature) while mitigating the risks of politicisation and bias?

The Commission also identified several potential ‘foundation’ reforms in the stage 2 Inquiry that could proceed regardless of the ultimate default allocation arrangements recommended. These included:

- the establishment of a centralised online service for members, employers and Government, building on the existing functionality of myGov and Single Touch Payroll
- a centralised clearing house administered by the ATO
- a proposed merger transparency framework
- the introduction of a first timer default mechanism.

The first of those proposals garnered broad support from participants. The remaining three proposals will benefit from further consideration and consultation with participants as part of the current stage 3 Inquiry. Attachment C (table 4) details selected participant comment on the model-specific features and the standalone reforms that the Commission will further consider in the stage 3 Inquiry.

OTHER REFORMS: GENERAL QUESTIONS FOR PARTICIPANTS

On the first timer default mechanism:

- *How could the mechanism be designed to mitigate against the risks of entrenching member disengagement and the risk of members remaining in inferior products?*

On the proposed centralised clearing house:

- *What would be the cost to set up this platform within the ATO? What is the scope to utilise existing infrastructure within the ATO in establishing this platform? What is the evidence that a single government provider would not have the capability to operate the service, or that such a provider would fail to keep pace with technological change?*
- *What would be the expected ongoing costs of service provision? Specifically, what is the scope to reduce costs over current arrangements due to economies of scale?*
- *How many operators are currently in the market for the provision of clearing-house services? To what extent do existing arrangements facilitate new entry and promote the exit of inefficient providers, and what is the evidence on recent entry and exit?*
- *What international experiences can be drawn on to provide insights into the merits of a centralised clearing house in the Australian system?*

On merger transparency:

- *Would elevating the level of disclosure that prospective merger parties are required to provide to APRA (such as following a memorandum of understanding between the parties) create material risks of discouraging merger activity?*
 - *Would a requirement for trustees' to disclose merger discussions that had proceeded past a specific point to its members retrospectively (such as in annual reports) strike the balance between transparency and incentives for trustees to enter into preliminary discussions prior to (and during) the due diligence phase? What should this specific point be? How else could the mechanism be modified to strike such a balance?*
-

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Attachment A: Additional evidence needs

Table 3 Main additional evidence needs and sources

<i>Evidence required</i>	<i>Expected evidence sources</i>
Investment returns	
Long-term net returns by asset class and by market segment	Purchase data from private research firms; seek data from regulators
Asset allocation	
Actual asset allocation in choice and default segments	Purchase data from private research firms
Ability of small funds to access investments through intermediaries	Survey funds; draw on reviews by others
Costs and fees	
Data on product-level fees, fee dispersion, fund costs for specific services, fund margins, trailing adviser commissions and fund/product switching costs	Purchase data from private research firms; survey funds
Costs and fees associated with outsourcing to related/unrelated parties	Construct datasets from information already disclosed by funds; seek data from regulators; purchase data from private research firms
Fund expenditure on marketing, member retention and member engagement	Construct datasets from information already disclosed by funds; survey funds
Availability and quality of information on fees and investment risks	Draw on reviews by others; surveys of funds and members
Contestability	
Height of barriers to entry arising from default rules and market impediments to funds accessing distribution channels	Survey funds; draw on reviews by others
Fund behaviour	
Funds' use of member information and behavioural finance lessons in product design; development and take-up of tailored products, member services and retirement income products	Survey funds; draw on fund disclosures
Fund governance	
Trustee board disclosure, capability and investment governance	Draw on reviews by others; survey fund CEOs; survey funds

Table 3 (continued)

<i>Evidence required</i>	<i>Expected evidence source</i>
Insurance	
Impact of insurance on retirement balances	Purchase data from private research firms; survey funds
Insurance cover by age band and market segment, existence and consolidation of duplicate policies, take-up in choice products	Purchase data from private research firms; survey members; seek data from regulators
Comparison of premiums inside and outside of superannuation and historical ratio of claims to premium revenue	
Effect of policy settings on social security costs to Government ^a	Purchase data from private research firms; request data from relevant government departments and agencies
Ease and extent of members opting out of insurance, amending cover or making claims	Survey members; purchase data from private research firms; draw on reviews by others
Funds' use of member information to provide default insurance cover	Survey funds
Effect of regulation	
For ASIC:	Draw on reviews by others
<ul style="list-style-type: none"> regulator monitoring and enforcement activity on inducements ongoing and predicted effect of RG97 on transparency of fee disclosure 	
For APRA:	Draw on reviews by others
<ul style="list-style-type: none"> effect of current successor fund transfer rules and likely effect of proposed guidelines on fund mergers regulator activity in ensuring that trustees discharge their obligations under the scale test regulator activity in ensuring that trustees discharge their obligations on bundled insurance 	
Member behaviour and knowledge	
Member account activity and account monitoring	Survey funds and members; draw on fund disclosures
Default and switching rates for funds, accumulation products and insurance	Seek data from regulators; survey members; purchase data from private research firms
Member knowledge and understanding, including superannuation and insurance literacy	Survey members

^a This question is not part of the stage 1 assessment framework and has been added to reflect the Terms of Reference for the stage 3 Inquiry.

Attachment B: The Commission's assessment framework⁵

Competition: system-level objective, assessment criteria and indicators

Assessment criteria	Indicators	Assessment methods	Expected data sources
Objective 5: Competition in the superannuation system should drive efficient outcomes for members through: <ul style="list-style-type: none"> • a market structure and other supply and demand-side conditions that facilitate rivalry and contestability • suppliers competing on aspects of value to members 			
C1. Is there informed member engagement?	<ul style="list-style-type: none"> • Financial literacy of members compared to an 'adequate' standard (input) • Member superannuation and insurance literacy[#] (input) • Member active account activity: <ul style="list-style-type: none"> • voluntary contributions • uptake of intrafund advice • changes to investment/insurance options* (input, behaviour) • Member account monitoring activity: <ul style="list-style-type: none"> • use of fund websites • use of online calculators • call centre enquiries* (input, behaviour) • Use of advisers by members and/or member intermediaries (input) • Fund expenditure on member education and engagement as a proportion of total marketing expenditure* (input) • Availability of meaningful and comparable information on fees, product features (including insurance) and risks[#] (input) • Fund and product switching costs for members (administrative, search and learning costs) and costs to opt out of insurance (input) 	<ul style="list-style-type: none"> • Trend analysis • Qualitative • Trend analysis • Trend analysis • Trend analysis • Trend analysis • Qualitative • Trend analysis; qualitative 	<ul style="list-style-type: none"> • Member surveys • Member surveys • Member surveys; fund disclosures; case studies • Member surveys; fund disclosures; case studies • Member surveys • Research firms; fund disclosures; fund surveys • Reviews by others; member surveys • Member surveys; research firms

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⁵ This assessment framework is a direct and unchanged excerpt from the stage 1 final report (PC 2016).

Competition (continued)

<i>Assessment criteria</i>	<i>Indicators</i>	<i>Assessment methods</i>	<i>Expected data sources</i>
C2. Are active members and member intermediaries able to exert material competitive pressure?	• Defined contribution members that do not have choice of fund (input)	• Trend analysis	• Regulator data
	• Size of the SMSF sector (funds and members) relative to institutional sector (output)	• Trend analysis	• Regulator data
	• Changes in market shares of funds (output)	• Trend analysis	• Regulator data
	• Switching rate between and within default and choice products and between institutional funds and SMSFs (behaviour)	• Trend analysis	• Member surveys; fund surveys; research firms
	• Default rates for funds, accumulation products and insurance (behaviour)	• Trend analysis	• Regulator data; member surveys
	• Fee dispersion* (output)	• Trend analysis	• Research firms; fund disclosures
C3. Is the market structure conducive to rivalry?	• Corporate fee discounts (output)	• Trend analysis	• Regulator data
	• Market concentration at wholesale and retail levels (Herfindahl-Hirschman Index and market shares of largest providers)* (output)	• Trend analysis	• Regulator data
C4. Is the market contestable at the retail level?	• Number of institutional funds (input)	• Trend analysis	• Regulator data
	• Height of barriers to entry — effect of default rules on market entry (input)	• Qualitative	• Fund surveys; case studies; reviews by others
	• Height of barriers to entry — market impediments to funds accessing distribution channels (input)	• Qualitative	• Fund surveys; case studies; reviews by others
	• Entries, exits and consolidations of funds [#] (behaviour)	• Trend analysis	• Regulator data; fund disclosures

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Competition (continued)

<i>Assessment criteria</i>	<i>Indicators</i>	<i>Assessment methods</i>	<i>Expected data sources</i>
C5. Are there material anticompetitive effects of vertical and horizontal integration?	<ul style="list-style-type: none"> • Proportion of administration and investment services provided in-house, outsourced to related parties and outsourced to unrelated parties (input) • Proportion of insurance services outsourced to related parties (input) • Switching between insourcing and outsourcing of wholesale functions by funds (behaviour) • Alignment in the structure of member fees and underlying costs[#] (output) • Cost and member fee differences from outsourcing services to related versus unrelated parties (output) • Transparency and efficacy of fee disclosure by funds, including for distinct services[#] (behaviour) 	<ul style="list-style-type: none"> • Trend analysis • Trend analysis • Trend analysis • Econometrics; qualitative • Trend analysis • Qualitative 	<ul style="list-style-type: none"> • Regulator data; fund disclosures; fund surveys • Regulator data; fund disclosures; fund surveys • Fund disclosures; fund surveys • Regulator data; fund disclosures; research firms • Fund surveys; regulator data; fund disclosures • Reviews by others
C6. Do funds compete on costs/price?	<ul style="list-style-type: none"> • Costs relative to assets and number of accounts by service (investment, administration and insurance services) and by market segment (input) • Fees relative to assets and number of accounts by service (investment, administration and insurance services) and by market segment (output) • Fund margins (output) • Investment management costs and fees by asset class compared to other countries* (output) • Alignment in the structure of member fees and underlying costs[#] (output) • Transparency and efficacy of fee disclosure by funds, including for distinct services[#] (behaviour) 	<ul style="list-style-type: none"> • Trend analysis • Trend analysis • Trend analysis • Trend analysis • Econometrics; qualitative • Qualitative 	<ul style="list-style-type: none"> • Regulator data; research firms; fund disclosures • Regulator data; research firms; fund disclosures • Research firms • Research firms; fund disclosures • Regulator data; fund disclosures; research firms • Reviews by others

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Competition (continued)

<i>Assessment criteria</i>	<i>Indicators</i>	<i>Assessment methods</i>	<i>Expected data sources</i>
C7. Are economies of scale realised and the benefits passed through to members?	<ul style="list-style-type: none"> • Unused scale economies at fund level* (output) • Entries, exits and consolidations of funds[#] (output) • Pass through of benefits from scale economies (wholesale and retail) to members* (output) • Alignment in the structure of member fees and underlying costs^{#*} (output) • Increased diversification due to growing scale (input) 	<ul style="list-style-type: none"> • Econometrics • Trend analysis • Econometrics • Econometrics; qualitative • Econometrics 	<ul style="list-style-type: none"> • Regulator data; research firms • Regulator data; fund disclosures • Research firms; fund disclosures • Regulator data; fund disclosures; research firms • Regulator data; research firms
C8. Do funds compete on member-relevant non-price dimensions?	<ul style="list-style-type: none"> • Number of accumulation products (aggregate and per fund)* (output) • Fund marketing expenditure (share of operating expenditure) (input) • Funds' use of member information to inform product design and pricing* (input) • Availability of meaningful and comparable information on fees, product features (including insurance) and risks^{#*} (input) • Member superannuation and insurance literacy^{#*} (input) 	<ul style="list-style-type: none"> • Trend analysis • Trend analysis • Qualitative • Qualitative • Qualitative 	<ul style="list-style-type: none"> • Regulator data • Regulator data; fund disclosures • Fund surveys; case studies • Reviews by others; member surveys • Member surveys
C9. Is there innovation and quality improvement in the system?	<ul style="list-style-type: none"> • Introduction of new retirement income products* (output) • Development and active take-up of tailored products and member services* (output) • Introduction of new methods of service delivery* (output) 	<ul style="list-style-type: none"> • Trend analysis • Trend analysis; qualitative • Trend analysis; qualitative 	<ul style="list-style-type: none"> • Fund surveys; fund disclosures; case studies • Fund surveys; fund disclosures; case studies • Fund surveys; fund disclosures; case studies
C10. Are outcomes improving at the system level?	<ul style="list-style-type: none"> • Growing voluntary consumption of superannuation services (investment, retirement products, advice and insurance) (output) • Member satisfaction and trust* (outcome) 	<ul style="list-style-type: none"> • Trend analysis • Trend analysis; qualitative 	<ul style="list-style-type: none"> • Regulator data • Member surveys

[#] Repeated indicator within competition. * Indicator is common to both competition and efficiency.

Efficiency: system-level objectives, assessment criteria and indicators

Assessment criteria	Indicators	Assessment methods	Expected data sources
Objective 1: The superannuation system contributes to retirement incomes by maximising long-term net returns on member contributions and balances over the member's lifetime, taking risk into account			
E1. Are long-term net investment returns being maximised over members' lifetimes, taking account of risk?	<ul style="list-style-type: none"> Long-term (5, 10 and 20 year) historical net investment returns from the system and market segments compared to benchmarks (output) Long-term (5, 10 and 20 year) historical net investment returns to specific asset classes from the system and market segments compared to benchmarks (output) Variance of historical net investment returns (over 5, 10 and 20 years) from the system and market segments compared to benchmarks (output) Proportion of default products that persistently underperform the benchmark (for 5 or more consecutive years) (output) 	<ul style="list-style-type: none"> Trend analysis Trend analysis Trend analysis Trend analysis 	<ul style="list-style-type: none"> Regulator data; research firms Research firms; regulator data Regulator data; research firms Regulator data; research firms
E2. Are costs incurred by funds and fees charged to members being minimised, taking account of service features provided to members?	<ul style="list-style-type: none"> Costs relative to assets and number of accounts by service (investment and administration) and by market segment (input) Fees relative to assets and number of accounts by service (investment and administration) and by market segment (output) Alignment in the structure of member fees and underlying costs* (output) Investment management costs and fees by asset class compared to other countries* (output) Relationship between investment fees and returns at system level and for market segments (output) Cost savings from SuperStream (output) Relationship between level of administration fees and quality of member services (output) Unused scale economies at fund level* (output) Pass through of benefits from scale economies (wholesale and retail) to members* (output) Fee dispersion* (output) 	<ul style="list-style-type: none"> Trend analysis Trend analysis Econometrics; qualitative Trend analysis Econometrics Trend analysis Qualitative Econometrics Econometrics Trend analysis 	<ul style="list-style-type: none"> Regulator data; research firms; fund disclosures Regulator data; research firms; fund disclosures Regulator data; fund disclosures; research firms Research firms; fund disclosures Regulator data; research firms Regulator data Research firms; member surveys Regulator data; research firms Research firms; fund disclosures Research firms; fund disclosures

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Efficiency (continued)

<i>Assessment criteria</i>	<i>Indicators</i>	<i>Assessment methods</i>	<i>Expected data sources</i>
E3. Do all types of funds have opportunities to invest efficiently in upstream capital markets?	<ul style="list-style-type: none"> • Asset allocation in small funds compared to large institutional funds (input) • Retail investment management costs compared to wholesale (input) • Minimum transaction values (input) • Ability of small funds to access investments through intermediaries (input) 	<ul style="list-style-type: none"> • Trend analysis • Trend analysis • Trend analysis • Qualitative 	<ul style="list-style-type: none"> • Regulator data • Research firms • Research firms • Reviews by others; member surveys
E4. Is the system effectively managing tax for members, including in transition?	<ul style="list-style-type: none"> • Average effective tax rates across market segments (output) • Tax flexibility as a motivation for establishing SMSFs (input) • Take-up rates of co-contributions and offsets (input) 	<ul style="list-style-type: none"> • Trend analysis • Qualitative • Trend analysis 	<ul style="list-style-type: none"> • Regulator data; research firms • Member surveys • Regulator data
E5. Are other leakages from members' accounts being minimised?	<ul style="list-style-type: none"> • Unpaid Superannuation Guarantee contributions (input) • Delayed Superannuation Guarantee contributions (input) • Number and value of lost accounts (output) • Trailing adviser commissions embedded in choice products and insurance[#] (output) • Unclaimed superannuation (output) 	<ul style="list-style-type: none"> • Trend analysis • Trend analysis • Trend analysis • Trend analysis • Trend analysis 	<ul style="list-style-type: none"> • Regulator data • Regulator data • Regulator data • Fund surveys • Regulator data

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Efficiency (continued)

Assessment criteria	Indicators	Assessment methods	Expected data sources
Objective 2: The superannuation system meets member needs, in relation to information, products and risk management, over the member's lifetime			
E6. Is the system providing high-quality information and intrafund financial advice to help members make decisions?	<ul style="list-style-type: none"> • Availability of meaningful and comparable information on fees, product features (including insurance) and risks* (input) • Member active account activity: <ul style="list-style-type: none"> • voluntary contributions • uptake of intrafund advice • changes to investment/insurance options* (input, behaviour) • Member account monitoring activity: <ul style="list-style-type: none"> • use of fund websites • use of online calculators • call centre enquiries* (input, behaviour) • Fund expenditure on member education and engagement as a proportion of total marketing expenditure* (input) • Funds' application of the lessons from behavioural finance to improve information provision and product design# (behaviour, output) • Number of accumulation accounts and consolidations (behaviour, output) • Member superannuation and insurance literacy** (input) 	<ul style="list-style-type: none"> • Qualitative • Trend analysis • Trend analysis • Trend analysis • Qualitative • Trend analysis • Qualitative 	<ul style="list-style-type: none"> • Reviews by others; member surveys • Member surveys; fund disclosures; case studies • Member surveys; fund disclosures; case studies • Research firms; fund disclosures; fund surveys • Case studies • Regulator data; member surveys • Member surveys
E7. Is the system providing products to help members manage risks over their life cycles and optimally consume their retirement incomes?	<ul style="list-style-type: none"> • Asset allocations by age cohort (across different market segments and products) (output) • Life-cycle MySuper products (number of products and members, and as a proportion of total assets under management) (output) • Development and active take-up of tailored products and member services** (output) • Introduction of new retirement income products** (output) • Drawdown rates in transition and retirement (output) • Funds' use of member information to inform product design and pricing** (input) • Member superannuation and insurance literacy** (input) 	<ul style="list-style-type: none"> • Trend analysis • Trend analysis • Trend analysis; qualitative • Trend analysis • Trend analysis • Qualitative • Qualitative 	<ul style="list-style-type: none"> • Research firms; regulator data • Regulator data • Fund surveys; fund disclosures; case studies • Fund surveys; fund disclosures; case studies • Regulator data • Fund surveys; case studies • Member surveys

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Efficiency (continued)

Assessment criteria	Indicators	Assessment methods	Expected data sources
E8. Are principal-agent problems being minimised?	<ul style="list-style-type: none"> Existing ratings of system-wide quality of governance (input) Meaningful disclosure by trustee boards of: <ul style="list-style-type: none"> trustee directors' and investment committee members' qualifications and relevant skills/experience remuneration structures potential conflicts of interest due to related-party dealings and competing duties (behaviour) Quality of investment committee and investment governance processes, including use of performance attribution analysis and risk management (input) Member satisfaction and trust* (outcome) Proportion of complaints to the Superannuation Complaints Tribunal which are successful# (output) Proportion of funds that target short-term performance relative to their peers (behaviour) Degree of similarity in asset allocation among default products with different member characteristics (average age and balance) (input) 	<ul style="list-style-type: none"> Qualitative Qualitative Qualitative Trend analysis; qualitative Trend analysis Qualitative; trend analysis Trend analysis 	<ul style="list-style-type: none"> Reviews by others Reviews by others Reviews by others; fund surveys Member surveys Regulator data Research firms; fund disclosures; fund surveys Regulator data; research firms
Objective 3: The efficiency of the superannuation system improves over time			
E9. Does the system overcome impediments to improving long-term outcomes for members?	<ul style="list-style-type: none"> Introduction of new retirement income products** (output) Development and active take-up of tailored products and member services** (output) Introduction of new methods of service delivery* (output) Number of accumulation products (aggregate and per fund)* (output) Funds' application of the lessons from behavioural finance to improve information provision and product design# (behaviour, output) Impact of regulatory impediments on innovation (input) 	<ul style="list-style-type: none"> Trend analysis Trend analysis; qualitative Trend analysis; qualitative Trend analysis Qualitative Qualitative 	<ul style="list-style-type: none"> Fund surveys; fund disclosures; case studies Fund surveys; fund disclosures; case studies Fund surveys; fund disclosures; case studies Regulator data Case studies Case studies; fund surveys; reviews by others

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Efficiency (continued)

Assessment criteria	Indicators	Assessment methods	Expected data sources
E10. Are there material systemic risks in the superannuation system?	<ul style="list-style-type: none"> Market concentration at wholesale and retail levels (Herfindahl-Hirschman Index and market shares of largest providers)* (output) Degree of interconnectedness between upstream service providers and funds (input) Levels of leverage in SMSFs (input) 	<ul style="list-style-type: none"> Trend analysis Qualitative Trend analysis 	<ul style="list-style-type: none"> Regulator data Regulator data; research firms; reviews by others Regulator data
Objective 4: The superannuation system provides value for money insurance cover without unduly eroding member balances			
E11. Do funds offer value for money insurance products to members?	<ul style="list-style-type: none"> Duplicate insurance policies (output) Rates of insurance take-up in choice products relative to default products (output) Member superannuation and insurance literacy** (input) Ease of members opting out of insurance, amending cover or making claims (input) Number of members changing or opting out of default insurance cover (input) Funds' use of member information to inform product design and pricing** (input) Comparability of insurance product information disclosed by funds (input) Average insurance cover by age band and market segment (output) Proportion of complaints to the Superannuation Complaints Tribunal which are successful# (output) Number of members that nominate beneficiaries (input) 	<ul style="list-style-type: none"> Trend analysis Trend analysis Qualitative Qualitative Trend analysis Qualitative Qualitative Trend analysis Trend analysis Trend analysis 	<ul style="list-style-type: none"> Member surveys Regulator data; research firms Member surveys Member surveys; reviews by others Research firms Fund surveys; case studies Reviews by others; research firms Research firms Regulator data Member surveys; fund surveys; research firms

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Efficiency (continued)

<i>Assessment criteria</i>	<i>Indicators</i>	<i>Assessment methods</i>	<i>Expected data sources</i>
E12. Are the costs of insurance being minimised for the level and quality of cover?	<ul style="list-style-type: none"> • Insurance premiums inside compared to outside superannuation for like policies (output) • Insurance expenses (incurred by funds) (input) • Insurance premiums paid by members as a percentage of Superannuation Guarantee contributions made by insured members (output) • Ratio of claims to premium revenue (loss ratio) within superannuation over 5 and 10 year periods (output) • Fee and premium differences from outsourcing insurance services to related versus unrelated parties (output) • Proportion of APRA-regulated institutional funds switching their insurance provider (input) • Trailing adviser commissions embedded in choice products and insurance[#] (output) 	<ul style="list-style-type: none"> • Trend analysis • Trend analysis • Trend analysis • Trend analysis • Trend analysis • Trend analysis • Trend analysis 	<ul style="list-style-type: none"> • Insurer disclosures; research firms • Regulator data; fund surveys • Regulator data • Regulator data • Fund surveys; regulator data; fund disclosures • Fund disclosures • Fund surveys

[#] Repeated indicator within efficiency. ^{*} Indicator is common to both competition and efficiency.

Attachment C: Standalone stage 2 reforms and a common feature of alternative default models for further consideration

Table 4 **Comments by participants on selected features in stage 2**

<i>Feature proposed</i>	<i>Comments by participants^a</i>
First timer default mechanism	<p>👍 Lifetime default would address account proliferation</p> <p>👎 A new job entrant's initial default product may not always best suit their long term-needs</p> <p>👎 It could entrench member disengagement and lead to them being left stuck in inferior products</p> <p>👎 A sole focus on first timers would unnecessarily slow the benefits stemming from reform of default arrangements</p> <p>➡ Members should be regularly prompted to reassess their current product</p>
ATO Centralised Clearing House	<p>👍 Centralised clearing house is low cost to run and a key factor in encouraging new entry by funds in New Zealand</p> <p>👎 It is unnecessary and wasteful given the introduction of SuperStream and Single Touch Payroll</p> <p>👎 There would be high costs in shifting to a new model</p> <p>It would introduce concentration and key person risk into the system</p> <p>👎 There are questions about whether the ATO is well placed or has the capacity to perform this role</p>
Merger transparency framework	<p>👎 Current arrangements are effective and early disclosure would discourage initial merger discussions between trustees</p> <p>➡ Elevated disclosure of merger discussions to APRA once an MOU is agreed between the parties</p> <p>➡ All default products subject to independent verification of compliance with the scale test</p> <p>➡ Disclosure to members of merger discussions that had proceeded past a specific point should occur retrospectively</p>
Selection body	<p>👍 Proposed principles for the body are generally sound</p> <p>👎 The selection process would not be independent from government — risk that it would become politicised, conflicted or there would be a perception of bias</p> <p>👎 The FWC is a more appropriate body to determine the eligibility of default funds and this process should be retained in the industrial relations system</p> <p>➡ The selection body needs to have representatives from employee, employer and consumer groups</p>

^a The comments are colour-coded as follows: 👍 support for the reform; 👎 concerns about the reform; ➡ proposed amendments to the reform that could be reconciled with the Commission's approach.

Sources: ACCI, sub. DR79; ACTU, sub. DR71; AIST, sub. DR 90; ASFA, sub. DR96; Australian Super, sub. DR60; BT, sub. DR67; CHOICE, sub. DR93; Deloitte, sub. DR61; First State Super, sub. DR84; FSC, sub. DR88; Grattan Institute, sub. DR82; HESTA, sub. DR70; ISA, sub. DR78; Link Group, sub. DR92; Mercer, sub. DR73; PwC, sub. DR85; QNMU, sub. DR57; Rice Warner, sub. DR87; trans., Sydney, pp. 92-93; United Voice DR97; WSSA, sub. DR81.

Attachment D: How to make a submission or comment

How to make a short form comment

To assist members wishing to contribute to this Inquiry, the Commission has established an online short comment facility on the Inquiry web page. Such comments would not be considered formal submissions, but the Commission might use them to inform its conclusions.

The comments will be published anonymously on the Inquiry web page, unless you indicate that you do not want the comment to be published. The Commission reserves the right to not publish material on its website that is offensive, potentially defamatory, or clearly out of scope for the inquiry in question.

How to prepare a submission

Submissions may range from a short letter outlining your views on a particular topic to a much more substantial document covering a range of issues. Where possible, you should provide evidence, such as relevant data and documentation, to support your views.

Generally

- Each submission, except for any attachment supplied in confidence, will be published on the Commission's website shortly after receipt, and will remain there indefinitely as a public document.
- The Commission reserves the right to not publish material on its website that is offensive, potentially defamatory, or clearly out of scope for the inquiry or study in question.

Copyright

- Copyright in submissions sent to the Commission resides with the author(s), not with the Commission.
- Do not send us material for which you are not the copyright owner — such as newspaper articles — you should just reference or link to this material in your submission.

In confidence material

- This is a public review and all submissions should be provided as public documents that can be placed on the Commission's website for others to read and comment on. However, information which is of a confidential nature or which is submitted in

confidence can be treated as such by the Commission, provided the cause for such treatment is shown.

- The Commission may also request a non-confidential summary of the confidential material it is given, or the reasons why a summary cannot be provided.
- Material supplied in confidence should be clearly marked 'IN CONFIDENCE' and be in a separate attachment to non-confidential material.
- You are encouraged to contact the Commission for further information and advice before submitting such material.

Privacy

- For privacy reasons, all **personal** details (e.g. home and email address, signatures, phone, mobile and fax numbers) will be removed before they are published on the website. Please do not provide these details unless necessary.
- You may wish to remain anonymous or use a pseudonym. Please note that, if you choose to remain anonymous or use a pseudonym, the Commission may place less weight on your submission.

Technical tips

- The Commission prefers to receive submissions as a Microsoft Word (.docx) file. PDF files are acceptable if produced from a Word document or similar text based software. You may wish to research the Internet on how to make your documents more accessible or for the more technical, follow advice from Web Content Accessibility Guidelines (WCAG) 2.0<<http://www.w3.org/TR/WCAG20/>>.
- Do not send password protected files.
- Track changes, editing marks, hidden text and internal links should be removed from submissions.
- To minimise linking problems, type the full web address (for example, <http://www.referred-website.com/folder/file-name.html>).

How to lodge a submission

Submissions should be lodged using the online form on the Commission's website. Submissions lodged by post should be accompanied by a submission cover sheet.

Online*	http://www.pc.gov.au/inquiries/current/superannuation/assessment
Post*	Superannuation Productivity Commission Locked Bag 2, Collins St East Melbourne VIC 8003

* If you do not receive notification of receipt of your submission to the Commission, please contact the Administrative Officer.

Due date for initial submissions and comments

Please send submissions to the Commission by 21 August 2017.