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RE: Objectives of Superannuation Discussion Paper

PFS is pleased to provide this submission in response to Treasury's consultation on the proposed Objective of Superannuation initiated through its Discussion Paper dated 9 March 2016.

About PFS

PFS is a boutique consulting firm with deep actuarial and governance, risk and compliance experience in superannuation. Our clients include corporate, industry, and retail superannuation funds, as well as employer sponsors of superannuation arrangements.

Superannuation and Financial Security

The objective of superannuation as proposed by the FSI focuses exclusively on post-retirement income. We suggest there is merit in defining the objective more broadly as the provision of financial security, with the primary focus being post-retirement income but a subsidiary objective of providing financial security before retirement by providing benefits in certain circumstances in addition to, or instead of, those provided by the Commonwealth.

It is clearly appropriate that the primary objective relates to provision of post-retirement income. However it is also appropriate that there be some limits or arrangements to prevent the superannuation system being used to accumulate wealth on a tax-advantaged basis well beyond that required to provide any reasonable level of post retirement income. As the Government has already commented on this aspect we will not address it further.

The provision of death and disability benefits before retirement is an important and valued element of the current system. In relation to APRA regulated funds the RSE Licensee may offer life insurance (including disability), however where an RSE Licensee offers a MySuper product there is a requirement under the SIS Act to provide cover for all MySuper members. To ensure that insurance arrangements adequately address the minimum requirements of the legislation APRA has issued Prudential Standard SPS 250 - Insurance in Superannuation.

Ignoring this important aspect in the debate may result in an objective that is too narrowly defined and misses some of the key benefits that the existing system provides – and it could be argued that the requirement for MySuper products to offer insurance is actually inconsistent with the objective as proposed.

A standard feature of most superannuation funds with more than 4 members accepting employer contributions is coverage for Death and/or Total and Permanent Disablement of a member. This insurance cover provides a substitute lump sum or an income stream to either:

- the member of the fund in the event of their disablement or
- the beneficiary/ies, in the event of the death of a member of a fund.

This cover is usually provided via a group life insurance policy entered into by the Trustee of the particular fund. The group arrangement permits insurance at a significantly lower cost than if each individual were to purchase cover on a retail basis. Of course if the cover were not available at group rates through a superannuation fund many individuals might not buy insurance outside their superannuation fund, with implications for the burden that may ultimately have to be borne by the state in the event of death or disablement of a principal income earner.

Where a member is earning and regular contributions are being made to a superannuation fund the cost of a reasonable level of death and disablement insurance can be borne without a very significant impact on the accumulated superannuation balance. However it is not appropriate that a superannuation balance which is accumulated primarily to provide financial security post retirement be consumed by insurance premiums, so some regulation is warranted in relation to the provision of insurance by a fund which is not receiving contributions for the member concerned.

Insurance that provides individuals with some financial security is already an integral part of the superannuation system and we suggest this be recognised as an objective, rather than being excluded from any statement of objectives.

Interpretation and the Objective

The discussion paper states that the objective, wherever it is ultimately located, will only be a guide to the policy-making process and will not affect interpretation or application of superannuation legislation by the courts.

It is difficult to see how this can work, since even if the objective were not written into relevant legislation, it could be considered part of the context of superannuation legislation and therefore could quite reasonably be used as an interpretive tool where the courts consider there is ambiguity.

If the goal of defining the objective is to facilitate long term and stable superannuation policies, then attempting to restrict its use as an interpretive tool could be counter-productive. Without an objective which affects interpretation or application of superannuation legislation there may still be scope for the frequent legislative and policy changes that have characterised the legislative and regulatory framework for superannuation.

Taking this view, it is worth at least considering locating the objective in legislation and giving it the necessary authority to be used as a tool to interpret other relevant superannuation legislation. This would go some way to reducing the current experience of constant legislative and policy changes. It would still of

course be open to parliament to change the objective, but that would occur in the context of a debate about the purpose of superannuation.

All changes, including those relating to tax concessions, would need to be considered in the light of this objective.

Sole Purpose Test

The sole purpose test is a defining feature of the current superannuation regulatory framework. The relationship between an objective specified for superannuation, regardless of where it is specified, and the existing sole purpose test (as contained in the SIS Act) should be carefully considered. There is a risk that without proper consideration the interaction between the objective and the sole purpose test could create ambiguity and uncertainty. It may be necessary to amend the sole purpose test provisions to ensure consistency between that test and the objective, or it may ultimately be better to replace the sole purpose test entirely with the new objective.

Regardless of the approach taken, the elements of the existing sole purpose test should be factored into the discussion about an objective. As funds have organised their businesses and benefits on the basis of the sole purpose test, any change to this test has fundamental implications for the superannuation system.

Yours sincerely,

A handwritten signature in black ink, appearing to read "John Newman". The signature is fluid and cursive, with a long horizontal stroke at the end.

John Newman FIAA
Managing Director