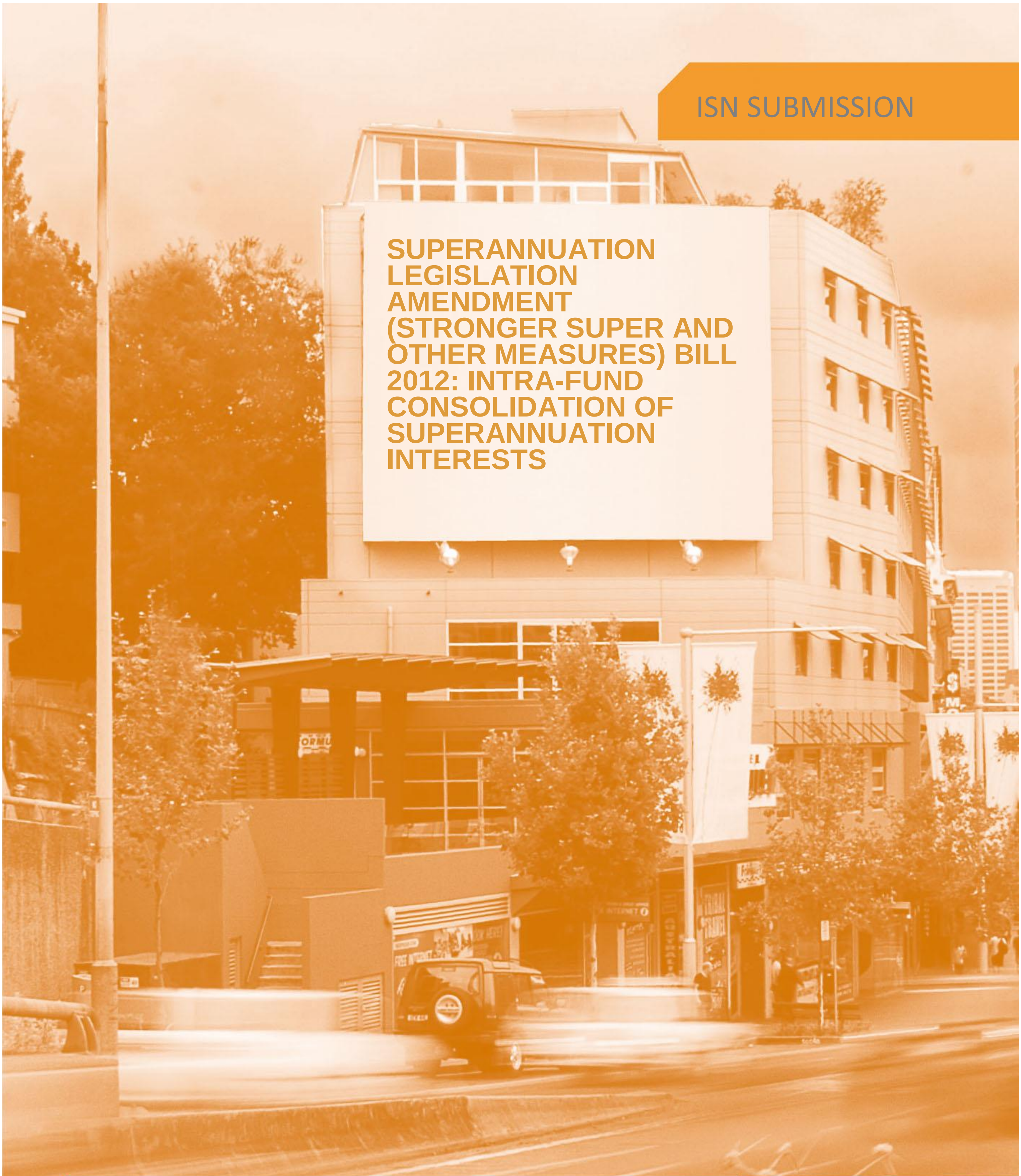
ISN SUBMISSION



SUPERANNUATION LEGISLATION AMENDMENT (STRONGER SUPER AND OTHER MEASURES) BILL 2012: INTRA-FUND CONSOLIDATION OF SUPERANNUATION INTERESTS

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About Industry Super Network

Industry Super Network (ISN) is an umbrella organisation for the industry super movement. ISN manages collective projects on behalf of a number of industry super funds with the objective of maximising the retirement savings of five million industry super members. Please direct questions and comments to:

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SUMMARY

ISN has significant reservations about the Superannuation Legislation Amendment (Stronger Super and Other Measures) Bill 2012: Intra-fund consolidation of superannuation interests (*the Bill*).

Whilst the objective of consolidating duplicate member accounts within a fund is a vital first step in broader inter-fund consolidation of multiple member accounts the proposed restrictions in the Bill will greatly reduce their effectiveness - specifically by only requiring funds to apply the intra-fund consolidation to:

- Accounts below $1,000
- Accounts that are inactive (2 yrs)
- Accounts without different benefits, notably insurance.

The $1,000 cap and restriction to accounts that had been inactive for two years were announced as Government policy only in relation to inter-fund account consolidation. These restrictions are inappropriate in the context of duplicate accounts in the *same* fund.

The different benefits clause has limited relevance in relation to intra-fund consolidation because members are not covered by life insurance multiple times within the same fund, even if they have multiple accounts. Where a member has one account with higher than default cover, this cover can be preserved through the account consolidation process.

It is consequently difficult to understand how any of these limits can be interpreted as being in the interest of members.

Multiple accounts within the same fund are mostly accidental. There are very few conceivable benefits to having multiple accounts within a fund, but there are clear and obvious costs, in the form of duplicate fees and insurance premiums.

After consulting with a number of large member funds ISN estimates the restrictions outlined in the Bill will result in as little as 15 percent of internal duplicate accounts being consolidated. Indeed it is likely that the provisions will achieve little more than what occurs at the moment with transfers of small balances to ERF's.

The proposed approach also has significant implications for the effectiveness of forthcoming inter-fund consolidation. In addition to the matters outlined above, suggestions during consultations of 'difficulties' in legislating for an opt-out framework will greatly diminish the potential of the measures to consolidate multiple accounts. This submission argues that there are clear legal precedents for 'opt-out' measures in retirement savings policies globally. Specifically the New Zealand 'Kiwi Saver' scheme operates on an 'opt-out' basis.

Accordingly ISN recommends that:

1. The proposed $1,000 account cap is removed;
2. The proposed inactive account requirement is removed (or significantly scaled back);
3. Consolidation is unaffected by different insurance arrangements, with Trustees required to preserve the higher level of cover;
4. The legal framework for the 'opt-out' arrangements associated with New Zealand's 'Kiwi Saver' are replicated to address any potential difficulties arising from consolidation of multiple accounts where there are product differences which a member may wish to retain.

1. Key Issues

As currently drafted a number of provisions in the Bill are excessively risk adverse and will significantly diminish the effectiveness of intra-fund consolidation.

Specifically a number of the proposed limitations to consolidate accounts implicitly assume a member may have deliberately established multiple accounts in the same fund for some unspecified advantage, and legislated consolidation of these accounts would diminish a member's benefits and rights.

Such an assumption (if made) has little or no basis in fact. It ignores the reality that most multiple accounts arise when an employee is newly engaged in a workplace which has a default fund which the member already has an interest in, and, for one reason or another, the fund does not recognise that the member already has an interest.

Multiple accounts in the same fund do not provide any potential 'trustee diversification' benefit, and multiple insurance cover is typically unavailable. Multiple accounts within the same fund significantly increase costs for members but do not confer additional benefits. This submission discusses a number of the key issues that need to be resolved in order that the intra-fund consolidation provisions be effective.

2. Proposed $1,000 Account Threshold

The first restriction limits the consolidation to accounts of less than $1,000. No rationale is given for the threshold, though this limit had previously been raised in the context of *inter*-fund consolidation.

Such a threshold if adopted will result in less than 30% of duplicate accounts within the same fund being consolidated. Coupled with the inactive account restriction discussed below consolidation would be half this again.

Such a threshold for intra-fund consolidation is unreasonably low and arguably will achieve little more than the existing ERF arrangements. With a threshold set at such a low level an account created for a spell of work of just 10 weeks at average earnings wouldn't be consolidated.

2.1 Recommendation – Account Threshold

> For intra-fund consolidation there should be no threshold applied for consolidation to occur.

The $1,000 cap, as suggested in the context of inter-fund consolidation, is described as a first step, before the limit is increased to $10,000, and possibly higher levels. However, to make the limit explicit in legislation, rather than having the amount described in subordinate regulation, obviously requires legislative change to have the limit increased, clearly adding further uncertainty to delivery on the stated policy.

Any dollar based limits to minimum required inter-fund consolidations should therefore be detailed in regulation rather than legislation.

3. Inactive account definition

The limitation to inactive accounts (2 yrs) emerged in discussion around *inter*-fund consolidation to deal with the (admittedly exceptional case) of seasonal workers who would often make contributions in burst up to 13 months apart. This is completely irrelevant to intra-fund consolidation. It will limit the consolidation by another 50%; ie, <u>to less than 15% of accounts</u>.

3.1 Recommendation – Inactive account definition

> For intra-fund consolidation the inactive account definition should be removed or the duration shortened significantly.

4. Insurance and other product differences

Different insurance arrangements between accounts has been raised in the context of inter-fund consolidation. It has been argued that a member may choose to have multiple accounts to maximise insurance coverage.

These arguments, while tenuous in the context of multiple accounts between funds, are irrelevant in the context of multiple accounts within a single fund.

Multiple insurance is extremely rare within the fund. In practice, many members are simply paying double for the same cover, and most will not receive any benefit (or even compensation) for that cost.

People may have multiple interests including an interest in a corporate division with superior benefits, but then (in their best interest) all their entire holdings should be consolidated into the superior product.

People may have one account with above default levels of insurance; again, the accounts can be consolidated and the higher level of insurance maintained.

4.1 Recommendation – Product differences

In the context of multiple intra-fund accounts trustees should be obligated to consolidate accounts such that the interests of the member are maximised. In most instances this would require the trustee to preserve a higher level of insurance coverage or other benefits and minimise admin and investment fees (such that any differences exist between multiple accounts in the same fund).

5. 'Opt-out'

During consultations with Treasury on the Bill there was a suggestion that there may be difficulties in legislating for an opt-out basis for consolidation.

'Opt-out' emerged during the SuperStream consultations as the most effective way to deal with the limited circumstances where a member may wish to maintain multiple accounts between funds (for diversification or to satisfy their insurance needs).

It was envisaged that consolidation of multiple accounts would proceed unless the member opted-out. Alternatively the opt-out notice would serve as an appropriate prompt for the member to consider the features of the consolidated product (including adjusting insurance coverage if required).

These arrangements were proposed due to the lack of effectiveness of existing arrangements where members must explicitly consent to the consolidation of multiple accounts.

Whilst there are limited examples of 'opt-out' provisions in Commonwealth legislation there are examples in other jurisdictions in the context of retirement income policy. Specifically New Zealand's 'Kiwi Saver' automatically enrols new employees in the scheme unless they 'opt-out' within a six week window (http://www.kiwisaver.govt.nz/new/opt-out/).

Further information can be found in Part 2 of the Kiwi Saver Act 2006 (http://www.legislation.govt.nz/act/public/2006/0040/latest/DLM378372.html).

Without effective opt-out arrangements and only limited exceptions the multiple account consolidation benefits claimed by the Cooper Review and the Government will not be realised, and multiple accounts will continue to be an intractable problem which continues to diminish retirement savings.

5.1 Recommendation – 'opt-out'

That an opt-out legal framework be adopted to allow members the opportunity to consider any differences between multiple accounts including being given the choice to prevent any consolidation or use the advice to modify product features of the consolidated account once it is completed. The provisions used for New Zealand's Kiwi Saver could, with some modification, be replicated for this purpose.