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Shibani Iyer
Director, Member Outcomes and Governance Branch
Retirement, Advice and Investment Division
The Treasury
Langton Crescent
Parkes ACT 2600

[By Email: superannuation@treasury.gov.au](mailto:superannuation@treasury.gov.au)

Dear Ms Iyer,

Superannuation Performance Test Treatment of Faith-based Products

The Financial Services Council (**FSC**) welcomes the opportunity to comment on the Exposure Draft *Treasury Laws Amendment (Measures for a later sitting) Bill 2022: Faith-based products (Draft Legislation)* to adjust how faith-based superannuation products are treated under the annual performance test.

The FSC is a peak body which sets mandatory Standards and develops policy for more than 100 member companies in one of Australia's largest industry sectors, financial services.

Our Full Members represent Australia's retail and wholesale funds management businesses, superannuation funds, life insurers and financial advice licensees. Our Supporting Members represent the professional services firms such as ICT, consulting, accounting, legal, recruitment, actuarial and research houses.

We understand the changes proposed under the Draft Legislation are intended to be specific for superannuation funds of a religious affiliation that have a MySuper offering and so are not immediately relevant to the FSC's superannuation membership.

Our comments are therefore made in the broader context of performance testing where we have long advocated for the performance testing of superannuation products to appropriately reflect investment performance, product goals and objectives, and member experience.

Overall, we support the important precedent the Government will be setting to recognise that the standard benchmarking approach to measuring performance of MySuper products is not appropriate in a range of circumstances, including religious affiliation and that offer MySuper products designed, operated and disclosed in line with religious values.

Importantly, appropriate performance testing, in driving additional accountability on the investment performance of superannuation trustees, should not undermine the overarching notion of superannuation member directed choice.

We note the question of how to extend performance testing to other superannuation products will be consulted on shortly as part of Treasury's review of the Your Future, Your Super laws. Towards this objective, we make a number of comments on the principles underlying the adjustments proposed to the performance test for faith-based products.

Active Investor Choice

Our defined contribution superannuation system is built around the notions of universality and also diversity. So, while the universality of Australia's superannuation system is reflected by the compulsion of contributions into the system through the Superannuation Guarantee, superannuation members can personally choose how they invest their money to generate an additional source of income in their retirement.

Like faith-based products, a superannuation member's decision to invest in one or more choice products may derive from their personal beliefs, goals and values. The retrospectively applied objective measured in the performance test will not align with client directed beliefs, goals and values in a number of circumstances. Specific examples, beyond faith based products include, ESG products, total return products, capital protected products, products designed to manage volatility and products designed specifically for income.

The precedent that will be set for faith-based products in practice is not distinguishable for many other forms of superannuation products. The issue is not whether the investment goals or objectives impact investment performance as measured against the performance test, but rather whether products are being assessed against metrics which reflect the objectives and strategy they are designed, operated and disclosed to deliver to their members.

We support the proposed approach of a supplementary test for faith-based funds as a way of holding the investment performance of trustees accountable without unduly penalising them for investing members' monies in accordance with their member's faith. However, once this precedent is set it must be expanded to Choice products in a reasonable way.

Greater regulator discretion

Broadly speaking, the draft legislation proposes greater regulator discretion for the administration of the annual performance test for faith-based MySuper products by empowering APRA to:

- Determine that a MySuper product is also a faith-based product; and
- Approve the use of a supplementary annual performance test for a faith-based product.

The FSC agrees with the principle of giving APRA more discretion in how to administer the performance test to resolve situations where applying a standard benchmarking approach would be inappropriate. In our view, this principle would also apply to non-MySuper products ('Choice' products) given their diversity in product features and investment strategies as compared to MySuper products.

Under the proposed approach for faith-based products, we note the onus would be on each trustee to provide the necessary evidence to demonstrate why its MySuper product should be treated differently under the annual performance test and for the trustee to propose a supplementary test.

While separately obtaining regulatory approval for a potentially different supplementary test may be viable for faith-based products given they are in limited number, we would support a more consistent and streamlined approach to performance testing across various segments of Choice products that meet certain, objective criteria to reduce the administrative burden on industry and on APRA. We expect this would be a matter for consultation in the review of the Your Future, Your Super laws.

Importance of disclosure

Under the proposed laws, in applying for faith-based status, the trustee must declare that the product used a faith-based investment strategy and that this is disclosed in its regulated disclosures and marketing materials.

Additionally, the Explanatory Materials to the Draft Legislation suggest that further application requirements which evidence effective disclosure may be specified in regulations and could include, for example, the product's Product Disclosure Statement and a copy of any advertising materials disclosing the product's faith-based investment strategy.

We support the proposed approach. These application requirements reflect an important role that disclosure of a superannuation product's investment strategy plays in enabling superannuation members to make informed decisions. This principle would apply equally to Choice products.

Failing the annual performance test

We note the proposed operation of the annual performance test for faith-based products would be adjusted so that the faith-based product would only fail the test if it does not satisfy the initial test and also the supplementary test. We would support this adjustment for the reason that disclosing to members of a faith-based product that their product has failed the initial test, but has passed the supplementary and more appropriate test, would be illogical and misleading.

We further note that the consequences of failing the annual performance test for faith-based products remain unchanged. We do not object to taking this approach for MySuper products. Where trustees fail to meet a defined standard of investment

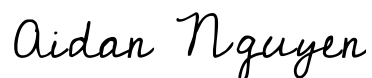
performance for their members, the consequences for underperformance should rightly ensure that new members can no longer be accepted, including by way of default, into the product until a subsequent test is passed.

Transparency

It will also be important for there to be transparency in APRA's publication of the results of the performance test. This should include publication of whether a fund was subject to a supplementary test and the benchmarks which applied to each product to allow consumers and their advisers to compare the metrics being used to assess each product's performance. Such a transparent approach would be consistent with the existing approach prescribed in legislation, where the benchmarks being used for each asset class are clearly defined and publicly available.

We would be happy to answer any questions you may have on this submission. Please feel free to contact me, Aidan Nguyen, on ANguyen@fsc.org.au.

Yours sincerely,



Aidan Nguyen
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